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TRANSCRIPT OF RECORD

Supreme Court of the United States

OCTOBER TERM, 1932

No. 791

IRENEE DU PONT, PETITIONER,

vs.

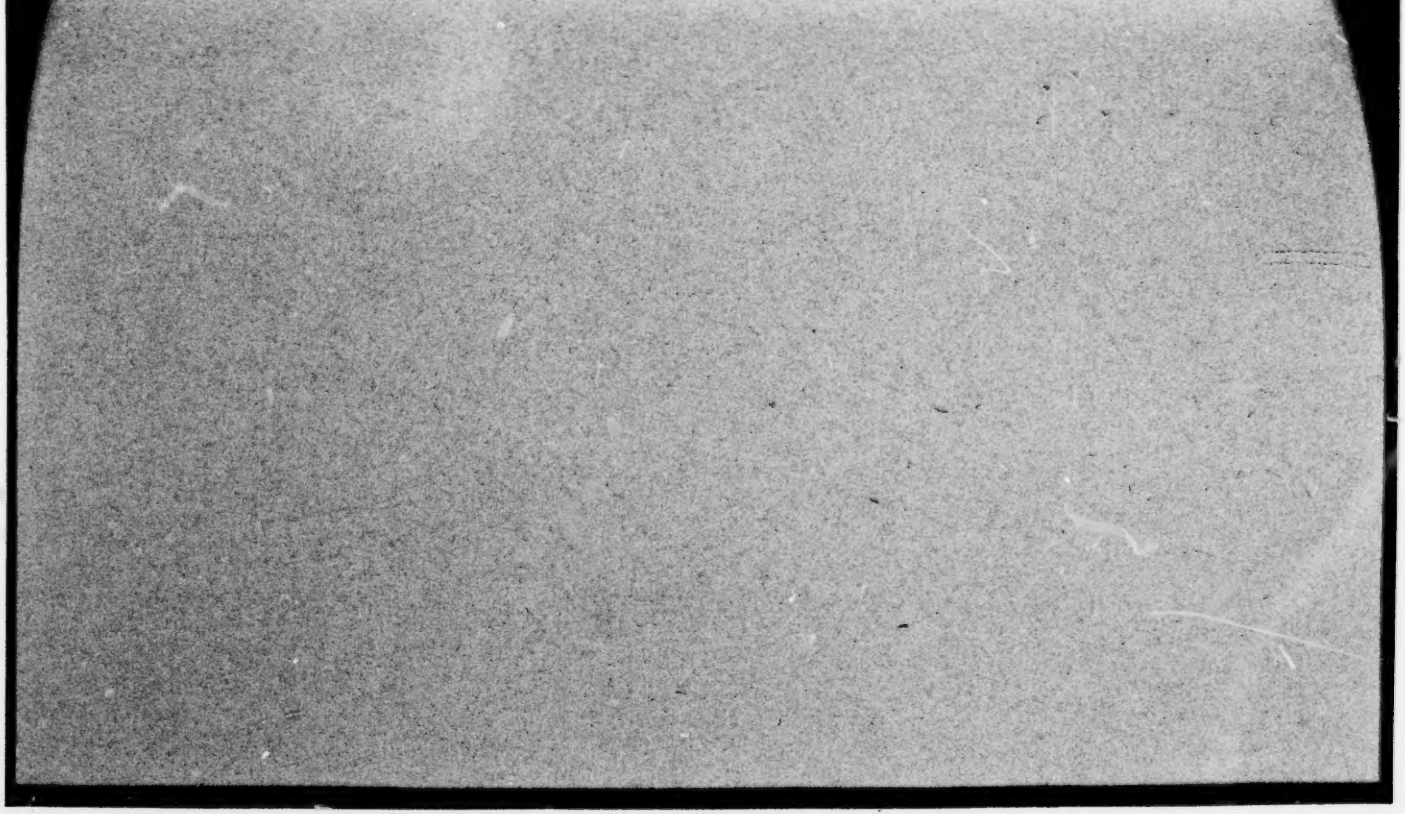
COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

PETITION FOR CERTIORARI FILED MARCH 20, 1933

CERTIORARI GRANTED MARCH 27, 1933

(37,488)



(37,488)

SUPREME COURT OF THE UNITED STATES

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COMMISSIONER OF INTERNAL REVENUE

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[fols. a & 1]

BEFORE UNITED STATES BOARD OF TAX APPEALS

Docket No. 31468

IRENEE DU PONT, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

Appearances:

For taxpayer: Kingman Brewster, Esq.; J. S. Y. Ivins, Esq.

For Commissioner: F. Shearer, Esq.

DOCKET ENTRIES

Nov. 7, 1928. Petition received and filed. Taxpayer notified. (Fee paid.)

Nov. 8, 1928. Copy of petition served on General Counsel.

Jan. 9, 1929. Answer filed by G. C.

Jan. 9, 1929. Copy served on taxpayer. General Calendar.

Jan. 27, 1930. Hearing set 3/19/30.

Mar. 20, 1930. Transcript of hearing 3/19/30 filed.

Mar. 19, 1930. Hearing had before Mr. Black, Div. 15 on merits. Amended answer filed. Brief due 5/15/30.

[fol. 2]

May 15, 1930. Motion for extension of time to May 22, 1930, to file brief, filed by taxpayer.

May 15, 1930. Motion granted.

May 15, 1930. Order extending time for filing respondent's brief to May 22, 1930, entered.

May 19, 1930. Brief filed by G. C.

May 22, 1930. Brief filed by taxpayer.

Aug. 6, 1930. Findings of fact and opinion rendered. Eugene Black, Div. 15. Judgment will be entered for the respondent.

Aug. 7, 1930. Decision entered. Div. 15, Mr. Black.

Feb. 4, 1931. Motion to fix amount of bond, filed by taxpayer.

Feb. 4, 1931. Order fixing amount of bond at $50,000.00, entered.

Feb. 6, 1931. Supersedeas bond for $50,000.00 approved and ordered filed.

Feb. 7, 1931. Petition for review to U. S. Circuit Court of Appeals (3) with assignments of error filed by taxpayer.

Feb. 14, 1931. Proof of service filed.

Mar. 20, 1931. Motion for enlargement of time to 5/15/31 to prepare and transmit record filed by taxpayer.

Mar. 21, 1931. Order enlarging time to May 15, 1931, for preparation of evidence and delivery of record entered.

Apr. 28, 1931. Præcipe filed. Proof of service thereon.

[fol. 3] BEFORE UNITED STATES BOARD OF TAX APPEALS

[Title omitted]

PETITION—Filed November 7, 1928

The above-named petitioner hereby applies for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency (symbols IT:AR:B-4-HBA) dated September 8, 1928, and as a basis of his proceeding alleges as follows:

1. The petitioner is an individual with his address at Granogue, Delaware. His tax returns for the years herein involved were filed with the Collector of Internal Revenue at Wilmington, Delaware.

2. The notice of deficiency (a copy of which is attached and marked Exhibit A) was mailed to the petitioner on or after September 8, 1928.

3. The taxes in controversy are income taxes and surtaxes for the calendar years 1924, 1925 and 1926, and for $50,000.

[fol. 4] 4. The determination of tax set forth in the said notice of deficiency is based upon the following error:

(a) The Commissioner has erroneously included in income for 1924 dividends of $50,422.40, for 1925 dividends of $50,370.10, and for 1926 dividends of $50,422.40, which were received by the Wilmington Trust Company, Trustee, under irrevocable trusts created by the petitioner in the year 1923 and used by the trustee in the payment of premiums on insurance policies on the life of the petitioner.

5. The facts upon which the petitioner relies as the basis of this proceeding are as hereinbefore stated and as follows:

(a) The petitioner herein, during 1923, entered into agreements with the Wilmington Trust Company, of Wilmington, Delaware, under the terms of which certain securities were transferred and delivered to the Wilmington Trust Company as trustee, the income from such securities to be used to pay premiums on insurance policies upon the life of the petitioner.

(b) The petitioner under the aforesaid trust agreements irrevocably divested himself for the terms of the trusts of the ownership and possession of the property so transferred, and could not avail himself of any of the gain therefrom.

(c) At the time the aforesaid trust agreements were entered into it was recognized that under the provisions of the Revenue Act of 1921, then in force, income used as aforesaid for the purpose of paying insurance premiums was taxable to the recipient of such income, i. e., the trustee.

[fol. 5] (d) During the year 1924 dividends from securities transferred amounting to $50,422.40 were received by the trustee and, pursuant to the terms of the trusts, were used to pay insurance premiums. During the year 1925 dividends amounting to $50,370.10 and during the year 1926 dividends amounting to $50,422.40 were so received and applied.

(e) The dividends as aforesaid were returned as taxable income for the respective years by the trustee, whereas the Commissioner in his deficiency notice heretofore mentioned, has added the dividends as taxable income to the petitioner.

Wherefore the petitioner prays that this board may hear the proceeding, reverse the error in the Commissioner's audit and redetermine such deficiency or overpayment for each year as the facts and law warrant.

Kingman Brewster, Counsel for Petitioner, c/o Holmes, Brewster & Ivins, 815 Fifteenth Street N. W., Washington, D. C.

[fol. 6] *Duly sworn to by O. R. Folsom-Jones. Jurat omitted in printing.*

[fol. 7] EXHIBIT "A" TO PETITION

Treasury Department, Washington

Office of Commissioner of Internal Revenue

September 8, 1928.

Mr. Irenee du Pont, Granogue, Delaware.

SIR: In accordance with Section 274 of the Revenue Act of 1926 you are advised that the determination of your tax liability for the years 1924, 1925 and 1926 discloses a deficiency of $33,632.90, as shown in the attached statement.

The section of the law above mentioned allows you to petition the United States Board of Tax Appeals within sixty days from the date of the mailing of this letter for a redetermination of your tax liability. However, if you acquiesce in this determination, you are requested to execute the enclosed Form 866 and forward both original and duplicate to the Commissioner of Internal Revenue, Washington, D. C., for the attention of IT:C:P-7.

Respectfully, D. H. Blair by (S.) Wm. T. Sherwood,
Acting Deputy Commissioner.

Enclosures: Statement, Form 866, Form 882.

(Form 7928.)

[fol. 8] Statement

IT:AR:B-4. HBA-60D.

In re Mr. Irenee du Pont, Granogue, Delaware

Year	Deficiency in tax
1924	$16,955.37
1925	6,476.22
1926	10,201.31
Total	$33,632.90

The adjustments recommended in the reports of the Internal Revenue Agent in Charge, Baltimore, Maryland, have been approved with the following exceptions:

For the year 1925, the tax originally assessed was reported as $107,107.38, representing the original assessment of $109,194.07, less an overassessment of $2,086.69. Inasmuch as the records of this office disclose no overassessment previously allowed, the amount of $109,194.07 has been applied against your correct tax liability.

1924

Ordinary net income shown on return	$461,336.75
Add: 1. Increase in dividends	40,142.55
Ordinary net income adjusted	$501,479.30
Capital net gain reported	$2,549.90
Add: 2. Liquidating dividend	10,279.85
Capital net gain adjusted	$12,829.75

[fol. 9] Computation of Tax

Ordinary net income adjusted		$501,479.30
Less:		
Dividends	$531,819.58	
Personal exemption	2,800.00	
		534,619.58
Income subject to normal tax		None
Surtax on $501,479.30		$170,611.72
Tax at 12½% on $12,829.75		1,603.72
Total Tax		$172,215.44
Less: Tax paid at source		5.00
Tax assessable		$172,210.44
Tax previously assessed		155,255.07
Deficiency		$16,955.37

Explanation of Changes

1. Reference is made to your protests against the action of the examining officer in including in gross income dividends of $50,422.40, representing income received by the

Wilmington Trust Company, Trustee, under trusts created by you and used by the trustee in the payment of premiums on insurance policies covering your life.

You contend that none of the income of the trust should be included in your net income inasmuch as you did not at any time, alone or in conjunction with any person not a beneficiary of the trust, have the power to revest in yourself title to any part of the corpus of the trust; that the provisions of Secton 219 (h) of the Revenue Act of 1924 are not applicable to an irrevocable trust created prior to the passage of the Act; and that your case is analogous to that of a tax on transfers of assets.

[fol. 10] You are advised that Section 219 of the Revenue Act of 1924 contains no provision that it is applicable only to trusts or estates created subsequent to passage thereof; on the other hand; the section deals solely with the question of the taxability of income of estates or of any kind of property held in trust. Subdivision (h) of this section reads in part as follows:

"Where any part of the income of a trust is or may be applied to the payment of premiums upon policies of insurance on the life of the grantor (except policies of insurance irrevocably payable for the purposes and in the manner specified in paragraph (10) of subdivision (a) of section 214), such part of the income of the trust shall be included in computing the net income of the grantor."

The interpretation in Article 347 that "The income of such trusts must be so included whether or not the trust was created before the enactment of this act" was in accordance with Section 1101 which provides that the Commissioner, with the approval of the Secretary shall prescribe and publish all needful rules and regulations for the enforcement of the Act. In United States v. Johnston, 124 United States 236, Brown v. United States 133—United States 671 and other cases, the courts held that if such interpretation has been in effect for a long period without objection and particularly if it has been relied upon by taxpayers, it will be followed, if the statute does not clearly require a different interpretation.

Although the Revenue Act of 1921 did not tax the income of trusts similar to those under consideration to the grantors (the indirect beneficiaries of the trust income)

still that right reposed in Congress to be exercised at any time, irrespective of when the trust was created.

[fol. 11] In 1923, an obligation was assumed by you to pay the premiums on the policies of insurance that you had taken out on your life and, by setting aside a fund, the income of which was to relieve you of that burden, you continued to be none the less the beneficiary of the trust fund. Therefore, the income of the trust fund was indirectly your income in so far as it was applied to paying the premiums of life insurance.

For the last contention mentioned above, you rely on the decision of the courts in the case of Nichols v. Coolidge, in which it was held that Section 402 (c) of the Revenue Act of 1918 is unconstitutional in so far as it requires that there shall be included in the gross estate of the decedent, the value of the property transferred irrevocably in trust for the decedent before the enactment of the Revenue Act of 1918, merely because the conveyance was intended to take effect in possession or enjoyment at or after death.

You are advised, however, that the Bureau has consistently held that the estate tax and the income tax being entirely separate, the action taken for Federal estate tax purposes is not necessarily controlling for income tax purposes.

The action of the examining officer is, accordingly, sustained.

There was included in the dividends reported in your return $10,279.85, representing liquidating dividends which are taxable as capital gain under the provisions of Article 1545 of Regulations 65. The amount has, therefore, been eliminated from dividends.

The above adjustments result in a net increase in dividends of $40,142.55.

2. Your capital net gain has been increased by $10,279.85, liquidating dividends as explained above.

[fol. 12] 1925

Ordinary net income, adjusted by Collector	$544,477.52
Add: 1. Increase in dividends	50,370.10
	$594,847.62
Deduct: 2. Increase in contributions	17,980.00
Ordinary net income adjusted	$576,858.62

Less:		
Dividends	$620,269.43	
Personal exemption	5,500.00	
		625,769.43
Income subject to normal tax		None
Surtax on $576,858.62		$107,031.72
Tax on 12½% on $69,556.60		8,694.57
Total tax		$115,726.29
Less:		
Earned income credit	$55.00	
Tax paid at source	1.00	
		56.00
Tax assessable		$115,670.29
Tax previously assessed		109,194.07
Deficiency in tax		$6,476.22

Explanation of Changes

1. The increase in dividends by $50,370.10 represents the amount paid in this year by the Wilmington Trust Company on insurance policies covering your life. The item has been included in gross income for reasons as explained under a similar adjustment for the year 1924.

[fol. 13] 2. A deduction of $96,084.27 was previously allowed for contributions, whereas the correct amount is $114,073.27, representing 15% of your total net income.

1926

Ordinary net income shown on return		$1,331,066.99
Add:		
1. Increase in interest		467.33
2. Increase in dividends		50,422.40
Net income adjusted		$1,381,956.72
Less:		
Dividends	$1,343,168.66	
Personal exemption	5,500.00	
		1,348,668.66
Income subject to normal tax		$33,288.06

Normal tax at 1½% on $4,000.00	60.00
Normal tax at 3% on $4,000.00	120.00
Normal tax at 5% on $25,288.06	1,264.40
Surtax on $1,381,956.72	268,051.34
Tax on 12½% on $1,101,412.50	137,676.56
Total tax	$407,172.30
Less earned income credit	181.25
Tax assessable	$406,991.05
Tax previously assessed	396,789.74
Deficiency	$10,201.31

Explanation of Changes

1. The interest reported by you has been increased by $467.33 representing interest received on a refund of Federal income taxes.

[fol. 14] 2. The increase in dividends by $50,422.40 has been previously explained in this letter.

Payment should not be made until a bill is received from the Collector of Internal Revenue for your district, and remittance should then be made to him.

[fol. 15] Before United States Board of Tax Appeals

[Title omitted]

Answer—Filed January 7, 1929

Comes now the Commissioner of Internal Revenue, by his attorney, C. M. Charest, General Counsel, Bureau of Internal Revenue, and for answer to the petition of this taxpayer admits, denies and alleges as follows:

1. Admits the allegations contained in paragraph 1 of the petition.

2. Admits the allegations contained in paragraph 2 of the petition.

3. Admits the allegations contained in paragraph 3 of the petition.

4. Denies the allegations of error set forth in paragraph 4 of the petition.

5. Admits that during the years in question there was in force and effect a certain trust executed by the petitioner as grantor by the terms of which trust it was pro- [fol. 16] vided that the income should be applied on payment of premiums upon policies of insurance on the life of the petitioner, said policies of insurance being for purposes other than that specified in paragraph (10) (a) of Section 214 of the Revenue Acts of 1924 and 1926; that in the final determination the Commissioner included in the net income of the petitioner for the years in question certain amounts determined by the Commissioner to constitute that part of the income of said trust which was and which might be applied to the payment of premiums upon said policies of insurance on the life of said grantor; but for lack of sufficient information on which to form a belief denies all other allegations of fact contained in subparagraphs (a), (b), (c) and (e) of paragraph 5 of the petition. Admits the allegations contained in subparagraph (d) of paragraph 5 of the petition.

Denies each and every allegation of fact contained in the petition not hereinbefore specifically admitted, qualified or denied.

Wherefore it is prayed that the Commissioner's determination be approved and that the petition be dismissed and the appeal denied.

(Sgd.) C. M. Charest, General Counsel, Bureau of Internal Revenue. Of Counsel: F. R. Shearer, Special Attorney, Bureau of Internal Revenue.

[fol. 17] Before United States Board of Tax Appeals

[Title omitted]

Motion for Leave to Amend Answer—Filed March 19, 1930

Comes now the Commissioner of Internal Revenue, by his attorney, C. M. Charest, General Counsel, Bureau of Internal Revenue, and moves for leave to amend the answer filed herein January 7, 1929, and that said answer be considered as amended as follows:

In lieu of the prayer for relief contained in said answer, insert the following:

"Respondent, fully relying upon the correctness of the Commissioner's final determination, but as an alternative and partial defense in respect of the calendar year 1925 alleges that in the final determination by the Commissioner of the deficiency for the year 1925 petitioner was allowed a deduction for contributions in the total amount of $114,073.27 representing 15 per cent of the petitioner's total net income for said year; that the petitioner's net income for the year 1925 as determined by the Commissioner, after the allowance of said deduction of $114,073.27 for contributions, was $576,858.62 ordinary net income and $69,556.60 capital net gain; and that if the Board should redetermine the petitioner's net income to be less than the amount so [fol. 18] determined by the Commissioner the deduction for contributions should be recomputed at an amount which does not exceed 15 per centum of the taxpayer's net income as so redetermined without the benefit of said deduction.

"Wherefore, it is prayed that the Commissioner's determination be approved, that the petition be dismissed and the appeal denied, and (in the alternative) that the Board redetermine the correct deficiency for 1925."

(Sgd.) C. M. Charest, General Counsel, Bureau of Internal Revenue.

[fol. 19] Before United States Board of Tax Appeals

Docket No. 41368

Irenee du Pont, Petitioner,

v.

Commissioner of Internal Revenue, Respondent

Trust—Income—Insurance.—Where the petitioner created trusts and the income therefrom was used for the purpose of paying life insurance premiums on his own life the income of the trusts should be included in petitioner's income under Section 219 (h) of the Revenue Acts of 1924 and 1926.

Kingman Brewster, Esq., and J. S. Y. Ivins, Esq., for the petitioner.

F. R. Shearer, Esq., for the respondent.

Findings of Fact and Opinion—Filed August 6, 1930

Deficiencies in income tax and surtax were determined by respondent as follows: 1924, $16,955.37; 1925. $6,476.22; 1926, $10,201.31, amounting in all to $33,632.90. The petitioner created several trust funds the income from which was used to pay life insurance premiums on his own life. This income, amounting to $50,422.40 for 1924, $50,370.10 for 1925, and $50,422.40 for 1926, was added to that of peti- [fol. 20] tioner by respondent, thus creating the deficiencies and this is alleged to be erroneous by petitioner in asking redetermination.

FINDINGS OF FACT

The petitioner, under date of September 18, 1923, executed nine trust agreements for the benefit of his wife, their nine children, and other members and relatives of his family. These trusts were irrevocable for their duration, which was in the first instance until December 18, 1926, with provision for further extension upon notice by the trustor to the trustee. Two such notices have been given and the trusts have been extended to December 18, 1932.

By the trust agreements, the petitioner transferred to the Wilmington Trust Company, as trustee, the following properties:

(a) Thirty two insurance policies on the petitioner's life.

(b) Eight hundred and thirty shares of 7 per cent preferred stock of the Christiana Securities Company, a corporation existing under the laws of the State of Delaware.

The nine trust agreements were in full force and effect during the years 1924-1926, inclusive, and the 32 insurance policies were likewise in full force and effect and held under the terms of the trust during those years.

The transfer of the insurance policies was absolute and complete. By the trust instruments the trustee was made the owner of such policies and, if the trusts terminated prior to the petitioner's death, all interest in the policies would vest in certain named beneficiaries. The petitioner is not one of such beneficiaries.

[fol. 21] If the petitioner dies prior to December 18, 1932 (or such other date to which the trusts might further be extended), the proceeds of the life insurance policies are to become a trust fund in the hands of the trustee, designated as the Primary Trust Fund. The net income therefrom and the fund itself would be distributed and paid over to named beneficiaries, other than the petitioner or his estate, as indicated in the trust agreements.

The petitioner retains no right to change the beneficiaries under the insurance policies named in the trust agreements. He has no right to surrender the policies for the surrender values indicated therein, nor to borrow against them. There is no provision under which title to the policies could revest in the taxpayer either at his own discretion or that of nim co-jointly with anybody else.

As to the shares of stock transferred under the trust agreements, the trustee receives the income from the securities, applies the same to the payment of taxes, governmental charges, and incidental expenses including its commissions, and uses the balance of the income for the payment of premiums on the policies of life insurance for the period of the trusts, or so long as the petitioner lives, whichever is the shorter.

If the trusts terminate prior to the petitioner's death, the securities and any income not paid out, all of which is designated the Secondary Trust Fund, are to be transferred to the petitioner. If the petitioner dies prior to the end of the trusts, the securities and any net income thereon are to be distributed to the nine children or their issue in the manner specified therein. No part of the Secondary Trust Fund in such case, goes to the petitioner's estate.

Such is the combined substantive effect of the provisions of the nine trust agreements. To simplify the description of the separate interest of each child dependent upon con-
[fol. 22] tingencies, nine distinct trusts (each applying to a one-ninth share in the trust funds) are provided for.

During the year 1924 dividends from securities transferred to and held by the Wilmington Trust Company as trustee, amounting to $50,422.40, were received by such trustee and, pursuant to the terms of the trusts, were used to pay insurance premiums. During the year 1925 dividends amounting to $50,370.10 and during the year 1926 dividends amounting to $50,422.40 were so received and

applied. These amounts have been treated by the Bureau as income taxable to the petitioner and subject to income taxes and surtaxes under the Revenue Acts of 1924 and 1926. This action is based upon the Commissioner's interpretation of Section 219 (h) of the Revenue Acts of 1924 and 1926.

The petitioner's wife and all the children, beneficiaries of the trust, were living during the years 1924 and 1926, and are still living.

OPINION

Black: The taxable years involved in this proceeding are 1924, 1925 and 1926 and hence are governed by the Revenue Acts of 1924 and 1926. Under Section 219 of each of these Acts it is provided that the tax shall be computed upon the net income of the estate or Trust and shall be paid by the fiduciary, except under certain conditions prescribed in subdivisions (g) and (h) of said Section.

In this proceeding we are not concerned with subdivision (g) and only with that part of subdivision (h) which reads as follows:

Where any part of the income of a trust is or may be applied to the payment of premiums upon policies of insurance on the life of the grantor (except policies of insurance [fol. 23] irrevocably payable for the purposes and in the manner specified in paragraph (10) of subdivision (a) of section 214), such part of the income of the trust shall be included in computing the net income of the grantor.

The petitioner was the grantor of the trusts involved in this proceeding, the part of income of the Trust upon which the deficiencies are based was used to pay premiums on policies of insurance on the life of the grantor, and respondent has included such amounts in computing the net income of the grantor for the respective taxable years as is provided in Section 219 (h).

Petitioner attacks this determination of respondent on the following grounds: (1) subdivision (h) of Section 219 has no application to the income of an irrevocable trust; (2) even if the language of the subdivision does have application to an irrevocable trust, it does not have any application to an irrevocable trust created prior to the enactment of such subdivision; and (3) if said subdivision (h)

of Section 219 does have the application contended for by the Commissioner, it is unconstitutional and void because it is violative of the Fifth Amendment to the Constitution of the United States. Similar contentions have already been fully considered by the Board in Frederick B. Wells, 19 B. T. A. 1213, and Alfred F. Pillsbury, 19 B. T. A. 1229, and decided adversely to the contentions made by petitioner. See also Corliss v. Bowers, 281 U. S. 376.

Counsel for petitioner lay considerable stress in their brief on their contention that petitioner was under no obligation to pay premiums on the insurance policies assigned to the trustee, and that since the evidence shows that the policies had been irrevocably assigned to the trustee, the petitioner no longer had any interest in them. It is of course true that in an ordinary insurance policy, the in- [fol. 24] sured is under no legal obligation to pay the premiums due on a policy. If he fails to make the payments within the time prescribed in the policy, it lapses. But if he wants to keep the policies alive and in force he must make payment of the premiums. The policies of insurance involved in this proceeding were for the benefit of petitioner's wife and nine children. Evidently it was the desire of the petitioner to keep these policies alive and in full force. The expense involved in the payment of life insurance premiums by a husband and father on policies for the benefit of his wife and children is regarded as a personal expense by the internal revenue laws, and is not an allowable deduction in determining the net income of the taxpayer. If, by the method used in this proceeding, the petitioner can transfer to a trust the burden of paying these insurance premiums and secure the deduction that way, in so far as payment of surtaxes is concerned, then he has accomplished by indirect means that which the law would not permit him to accomplish directly. It was this sort of thing which Congress sought to prevent when it enacted the part of subdivision (h) of Section 219, Revenue Acts of 1924 and 1926, which we have quoted at the beginning of this opinion.

Under the authorities above cited,

Judgment will be entered for the respondent.

[fol. 25] BEFORE UNITED STATES BOARD OF TAX APPEALS, WASHINGTON

Docket No. 41368

IRENEE DU PONT, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

DECISION—Filed August 7, 1930

Pursuant to the board's findings of fact and opinion, promulgated August 6, 1930, it is

Ordered and decided that there are deficiencies as follows:

Year	Deficiency
1924	$16,955.37
1925	6,476.22
1926	10,201.31

(Sgd.) Eugene Black, Member United States Board of Tax Appeals.

[fol. 26] IN UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

[Title omitted]

PETITION FOR REVIEW OF THE DECISION OF THE UNITED STATES BOARD OF TAX APPEALS—Filed February 7, 1931

To the Circuit Court of Appeals for the Third Circuit:

Your petitioner, Irenee du Pont, respectfully shows:

I

This is a petition for review by the Circuit Court of Appeals of the Third Circuit of a decision of the United States Board of Tax Appeals promulgated August 6, 1930, and the final order in which was entered August 7, 1930, redetermining deficiencies in federal income taxes and/or surtaxes against the petitioner for the years 1924 to 1926, inclusive, in the following amounts:

[fol. 27] 1924	$16,955.37
1925	6,476.22
1926	10,201.31
Total	$33,632.90

II

Your petitioner resides in the County of New Castle in the State of Delaware and within the jurisdiction of the United States Circuit Court of Appeals for the Third Circuit.

III

The nature of the controversy before the Board of Tax Appeals was the determination of federal income and/or surtaxes under the Revenue Acts of 1924 and 1926 involving the question of whether Congress intended to, or could, under the Constitution, impose income taxes and/or surtaxes upon the petitioner with respect to dividends received by a trustee, under irrevocable trusts established by the petitioner, which dividends were applied by the trustee to the payment of premiums on policies of insurance on the petitioner's life.

IV

The errors committed by the Board of Tax Appeals upon which the petitioner relies as the basis for this proceeding are:

1. In holding that the petitioner maintained an interest in and/or received a benefit from policies of insurance absolutely and completely sold, assigned, transferred and set over unto the trustee by the trust indentures involved in [fol. 28] this case, and in not holding that the petitioner maintained no interest in and/or received no benefit from said policies of insurance.

2. In holding that Congress, by the enactment of subdivision (h) of Section 219 of the Revenue Acts of 1924 and 1926, sought to prevent the income, of the type of trust existing in this case, from being taxed to the fiduciary but instead sought to tax such income to the grantor of the trust,

and in not holding that Congress had no such intention but on the other hand intended to restrict the application of subdivision (h) of Section 219 of the Revenue Acts of 1924 and 1926 to revocable trusts the income from which is or may be applied to the payment of premiums upon policies of insurance on the life of the grantor.

3. In holding that subdivision (h) of Section 219 of the Revenue Acts of 1924 and 1926 applies to irrevocable trusts, the income from which is, or may be, applied to pay premiums upon policies of insurance taken out on the grantor's life, and in not holding that said section does not apply to such type of trusts.

4. In holding that subdivision (h) of Section 219 of the Revenue Acts of 1924 and 1926 applies to irrevocable trusts, the income from which is, or may be, applied to pay premiums upon policies of insurance taken out on the grantor's life, regardless of whether or not such irrevocable trusts were created prior to the enactment of such subdivision, and in not holding such distinction material.

5. In holding that subdivision (h) of Section 219 of the Revenue Acts of 1924 and 1926 is constitutional under the Fifth Amendment in so far as applied to the facts of this case, and in not holding that said section, so applied, is unconstitutional under such amendment.

[fol. 29] 6. In not holding that subdivision (h) of Section 219 of the Revenue Acts of 1924 and 1926, as applied to the facts of this case, is unconstitutional under Article 1, Section 9, of the Constitution.

7. In including in petitioner's taxable income for the year 1924 the sum of $50,422.40, for the year 1925 the sum of $50,370.10, and for the year 1926 the sum of $50,422.40, each amount representing income received by the trustee of the trusts, under consideration in this case, in the respective years involved, and in failing to exclude such amounts from the petitioner's income.

8. In finding deficiencies in federal income taxes and/or surtaxes in each of the years 1924, 1925 and 1926, and in failing to find that there were no deficiencies in petitioner's federal income taxes and/or surtaxes for such years.

Wherefore your petitioner prays that this Court may review the decision of the Board of Tax Appeals, reverse such decision, and direct the Board of Tax Appeals to enter a decision determining that there are no deficiencies in income taxes and/or surtaxes due from this petitioner for the years 1924, 1925 and 1926, and for such other and further relief as may to this Court appear proper in the premises.

(Sgd.) Kingman Brewster, Counsel for Petitioner, c/o Brewster & Ivins, 815 Fifteenth Street N. W., Washington, D. C.

[fol. 30] *Duly sworn to by O. R. Folsom-Jones. Jurat omitted in printing.*

[fol. 31] Before United States Board of Tax Appeals

[Title omitted]

Præcipe for Record—Filed April 28, 1931

To the Clerk of the United States Board of Tax Appeals:

You will please prepare, and within the time prescribed by law, therefore, or such time as extended by order of the Board of Tax Appeals, transmit and deliver to the clerk of the Circuit Court of Appeals for the Eighth Circuit, copies duly certified of the following documents:

1. Docket entries of all proceedings before the Board of Tax Appeals.

2. All pleadings before the Board of Tax Appeals.

3. Findings of fact, opinion and decision of the Board of Tax Appeals.

4. Petition for review.

5. This præcipe for the record.

[fol. 32] The foregoing to be prepared, certified and transmitted as required by law and the rules of the Circuit Court of Appeals for the Third Circuit.

J. S. Y. Ivins, Counsel for Petitioner, % Brewster, Ivins & Phillips, 815 15th Street N. W., Washington, D. C.

Receipt of service of a copy of the foregoing præcipe for the record is hereby acknowledged this twenty-eighth day of April, 1931.

(Sgd.) C. M. Charest, General Counsel, Bureau of Internal Revenue.

[fol. 33] Before United States Board of Tax Appeals

[Title omitted]

Order Enlarging Time—Filed March 21, 1931

Upon motion of counsel for petitioner and consent of counsel for the respondent, it is

Ordered that the time for preparation of the evidence and for transmission and delivery of the record sur petition for review of the above-entitled proceeding in the United States Circuit Court of Appeals for the Third Circuit be and it is hereby extended to May 15, 1931.

(Sgd.) Logan Morris, Member.

Dated Washington, D. C., March 21, 1931.

[fol. 34] Clerk's certificate to foregoing transcript omitted in printing.

[fol. 35] In United States Circuit Court of Appeals for the Third Circuit, October Term, 1931

No. 4620 (List No. 73)

Irenee du Pont, Petitioner,

vs.

Commissioner of Internal Revenue, Respondent

Appeal from the United States Board of Tax Appeals

Order Assigning Judges—Filed Dec. 3, 1931

And now, to-wit, this third day of December, A. D. 1931, it is ordered that Hon. Oliver B. Dickinson, District Judge for the Eastern District of Pennsylvania, and Hon. Nelson

McVicar, District Judge for the Western District of Pennsylvania, be, and they are hereby, assigned to sit in above case in order to make a full court.

J. Warren Davis, Circuit Judge.

[File endorsement omitted.]

[fol. 36] Minute entry of argument and submission, December 3, 1931, omitted in printing.

[fol. 37] In United States Circuit Court of Appeals for the Third Circuit, October Term, 1931

No. 4620

Irenee du Pont, Petitioner,

v.

Commissioner of Internal Revenue, Respondent

Petition for Review from the United States Board of Tax Appeals

Opinion—Filed January 6, 1933

Before Davis, Circuit Judge, and Dickinson and McVicar, District Judges

Davis, Circuit Judge:

This is a petition for review from an order of redetermination of the Board of Tax Appeals involving income taxes for 1924, 1925, and 1926. 20 B. T. A. 482.

On September 18, 1923, the petitioner executed nine trust agreements for the benefit of his family. According to the terms of the agreements, he transferred thirty-two policies insuring his life, and certain shares of stock, to the trustee. The trustee agreed to apply the income from the stock to the payment of the premiums on the insurance [fol. 38] policies and to defray the expenses of carrying the trusts, which were irrevocable for their term of duration with a provision for further extension, on notice by the grantor to the trustee, but it was optional whether or not the grantor would extend the term. The trusts expired,

for the first time, on December 18, 1926, and since that date he has twice ordered their renewal. The last extension expired on December 18, 1932.

If the trusts terminate before the death of the petitioner, all interest in the insurance policies will vest in certain beneficiaries of whom the petitioner is not one, but the stock will be returned to him. If the petitioner dies before the trusts terminate, the proceeds of the insurance policies will become a trust fund to be distributed under the terms of the agreement, and the stock likewise distributed to beneficiaries, other than the petitioner's estate named in the agreement.

The Commissioner of Internal Revenue, in accordance with his construction of section 219 (h) of the Revenue Acts of 1924 and 1926, treated the income of the trusts for the years 1924, 1925 and 1926 as taxable to the petitioner for those years. The Board of Tax Appeals approved the determination of the commissioner and entered its decision accordingly.

Section 219, which is the same in both acts, provides that the tax shall be computed on the net income of an estate or trust and shall be paid by the fiduciary with certain exceptions. One of these in subdivision (h) controls this case and is as follows:

"* * * where any part of the income of a trust is or may be applied to the payment of premiums upon policies of insurance on the life of the grantor [except policies of insurance irrevocably payable for the purposes and in the manner specified in paragraph (10) of subdivision (a) of section 214 (referring to charitable and philanthropic [fol. 39] gifts)] such part of the income of the trust shall be included in computing the net income of the grantor."

The petitioner contends that section 219 (h) is not applicable where the grantor of an irrevocable life insurance trust has parted with all rights and benefits under the trust prior to the Act; but that if Congress did intend it to apply, then section 219 (h) is unconstitutional under the facts of this case.

The petitioner, as above stated, executed trusts and assigned to the trustee a large amount of personal property, the income from which the trustee was to use to pay the premiums on policies of insurance on the life of the

grantor. The petitioner asserts that the statute does not apply because he divested himself of all interest in the trust funds and the insurance policies (for a period of three years). But "a trust" as used in the statute includes both revocable and irrevocable trusts with or without reserved powers in the grantor; and so any "trust" created by the grantor, if the income from it is or may be used to pay for insurance on his life, comes within the terms of the statute.

Section 219 (h) in full provides:

"Where any part of the income of a trust may, in the discretion of the grantor of the trust, either alone or in conjunction with any person not a beneficiary of the trust, be distributed to the grantor or be held or accumulated for future distribution to him, or where any part of the income of a trust is or may be applied to the payment of premiums upon policies of insurance on the life of the grantor (except policies of insurance irrevocably payable for the purposes and in the manner specified in paragraph (10) of subdivision (a) of section 214), such part of the income of the trust shall be included in computing the net income of the grantor."

[fol. 40] The first part of the paragraph explicitly applies to the reservation of some power in the grantor of the trust; and, in the disjunctive, the second part has no limitation or reservation. Paragraph (g) of this section provides that income must be taxable to the grantor when he retains the power to revoke the trust at any time during the year and revest title in himself. In view of paragraph (g), the second part of paragraph (h) would have no purpose if it applies to revocable trusts only.

The intention of Congress as expressed in the exception in paragraph (h) concerning policies of insurance irrevocably payable for the purposes of charity or philanthropy is clear and unambiguous.

This intention may further be gathered from the following report of the Senate Committee on Finance on the Revenue Act of 1924.

"Section 219: This section has been rewritten in order to secure clarity and to prevent the evasion of taxes by means of estates and trusts.

(1) It is provided in this section that in the case of a trust where the trustee has the discretion to distribute or not, the income is taxed to the beneficiary if distributed and to the trustee if not distributed. The wording of subdivision (b) has been changed (1) to except from its provisions specifically subdivisions (g) and (h) which lay down special rules in lieu of the general provisions of subdivision (b); (2) to permit as an additional deduction that part of the gross income which, pursuant to the terms of the will or deed, is to be used exclusively for the prevention of cruelty to children or animals, since contributions by individuals to organizations for these purposes are deductible under section 214 (a) (10).

* * * * * * *

(3) Subdivision (h) of this section provides that the income of a trust which may be distributed to the grantor [fol. 41] or which may be used for the payment of premiums upon policies of insurance on his life shall be included in the gross income of the grantor. Trusts have been used to evade taxes by means of provisions allowing the distribution of the income to the grantor or its use for his benefit. The purpose of this subdivision of the bill is to stop this evasion.

The provisions of the House bill have been altered to exclude from taxation to the grantor of a trust income thereof used to pay premiums on insurance policies which are irrevocably payable to the benevolent organizations described in section 214 (a) (10). A trust of this kind is a proper method of providing for a gift to such organizations, and since the income is being used for these benevolent purposes rather than for the grantor's personal benefit it should not be taxed to him."

Senate Report No. 398, 68th Congress, First Session, page 25. House Report No. 179, 68th Congress, First Session, page 21.

Congress clearly intended to tax the income of such trusts to the grantor. Did it exceed its powers in doing so? The settlor says it did because he had neither a legal nor equitable title in the trust fund nor in the policies insuring his life to the payment of the premiums on which the income of the fund was applied. He contends that the

income of the trust fund was not his and to make the income of an irrevocable trust created before the enactment of the Revenue Acts of 1924 and 1926 taxable to him raises such serious doubts as to the constitutionality of section 219 (h) that such a construction should be avoided. He believes that section 219 (h) should be construed to apply only to trusts created after the act became effective.

But taxing to the grantor the income derived from the trusts in this case comes directly within the terms of the statute. It does not directly offend against any provision [fol. 42] of the Constitution and is in line with the general policy of taxation of the government which is concerned not so much with the refinements of title and interpretation as it is with the prevention of escape from taxation. The power of taxation is a fundamental necessity of government. Congress intended to establish a complete scheme for taxing income which must be carried out with due regard to substantial and practical results and must not be restricted by mere legal fiction. Tylor v. United States, 281 U. S. 497, 503. Corliss v. Bowers, 281 U. S. 376, 378. Old Colony Trust Company v. Commissioner, 279 U. S. 716.

No matter what is said, when we look at the result of the several transactions, the petitioner's income is reduced by the amount of the income of the trust funds. He has postponed his command over funds and policies for three years. While he has neither power over, nor title to, the funds nor a direct financial interest in the insurance policies, yet he is profiting by the arrangement, for he has seen to it that the income is to be applied to a purpose which he desired and required. But for his resorting to these legitimate devices which have many favorable features other than the one upon which he now insists, he would have continued paying the premiums on the insurance. He applied for and obtained the policies. He has merely postponed his right for the term of the trusts to command the fund and to terminate the existence of the contracts of insurance. Meanwhile, it is neither the trustee nor the beneficiaries of the policies who actually enjoy the taxable income but the petitioner himself. In its opinion the Board of Tax Appeals said:

"The expense involved in the payment of life insurance premiums by a husband and father on policies for the bene-

fit of his wife and children is regarded as a personal expense by the internal revenue laws, and is not an allowable [fol. 43] deduction in determining the net income of the taxpayer. If, by the method used in this proceeding, the petitioner can transfer to a trust the burden of paying these insurance premiums and secure the deduction that way, in so far as payment of surtaxes is concerned, then he has accomplished by indirect means that which the law would not permit him to accomplish directly."

The tax provided by section 219 (h) is placed upon income earned by the trust securities in so far as it may be used by the trustee to pay premiums on insurance on the life of the grantor. The insurance policies forming the trust res, or part of it, must be on the life of the person who executed the trust. This case is not like Hoeper v. Tax Commissioner, 284 U. S. 206, where the Court held that a State could not require a husband to include his wife's separate income in computing his income tax. There the husband had not owned, controlled or had the right to expend the money for his benefit and the case turned on the point that A could not be taxed on the basis of B's property.

The petitioner would reject the uniform construction of the commissioner and the Board of Tax Appeals because he believes that it amounts to taxing him with respect to property which is owned by another and in which he has no interest and so amounts to taking property without due process of law. But as we have pointed out section 219 (h) places the burden of the tax where it belongs, that is, on the one to whom it is income. Since it is income to the grantor, it would hardly be questioned that requiring him to report it as his was an unreasonable exercise of the taxing power contrary to the Fifth Amendment.

Nor does it appear that the income of the trust fund applied to the insurance should not be taxable to the grantor for the reason that the trusts were created prior to the effec- [fol. 44] tive date of the Revenue Acts of 1924 and 1926. The subject of the tax is income earned in 1924, 1925 and 1926. The statute affects income earned in those years. It does not impose a tax retroactively but presently and prospectively. Corliss v. Bowers, supra. Nichols v. Coolidge, 274 U. S. 521, and Coolidge v. Long, 282 U. S. 582, relate to the taxing of transfers of property completed before the

passage of the taxing act. The tax in this case is upon income realized from a trust fund during the taxable year.

The order of the Board of Tax Appeals is affirmed.

Dickinson, District Judge, dissents.

A true Copy. Teste:

—— ——, Clerk of the United States Circuit Court of Appeals for the Third Circuit.

[fol. 45] IN UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT, OCTOBER TERM, 1931

No. 4620

IRENEE DU PONT, Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent

JUDGMENT—Filed Jan. 6, 1933

Appeal from the United States Board of Tax Appeals

This cause came on to be heard on the transcript of record from the United States Board of Tax Appeals and was argued by counsel.

On consideration whereof, it is now here ordered, adjudged, and decreed by this Court that the order or decree of the said Board of Tax Appeals in this cause be, and the same is hereby, affirmed.

Philadelphia, January 6, 1933.

J. Warren Davis, Circuit Judge.

[File endorsement omitted.]

[fol. 46] Clerk's certificate to foregoing transcript omitted in printing.

[fol. 47] SUPREME COURT OF THE UNITED STATES

ORDER ALLOWING CERTIORARI—Filed March 27, 1933

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Third Circuit is granted. And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

Endorsed on cover: File No. 37,488. U. S. Circuit Court of Appeals, Third Circuit. Term No. 791. Irenee du Pont, petitioner, vs. Commissioner of Internal Revenue. Petition for a writ of certiorari and exhibit thereto. Filed March 20, 1933. File No. 37,488.

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CHARLES ELM

In the Supreme Court of the United States

OCTOBER TERM, 1932

No. 791

IRENEE DU PONT, *Petitioner*

v.

COMMISSIONER OF INTERNAL REVENUE, *Respondent.*

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

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In the Supreme Court of the United States

OCTOBER TERM, 1932

No. ....

IRENEE DU PONT, *Petitioner*

v.

COMMISSIONER OF INTERNAL REVENUE, *Respondent.*

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

PETITION[1]

The undersigned, on behalf of Irenee du Pont, of Granogue, Delaware, respectfully prays that a writ of certiorari issue to review the final decree of the Circuit Court of Appeals for the Ninth Circuit, entered January 6, 1933, in a proceeding therein entitled *Irenee du Pont* v. *Commissioner of Internal Revenue,* No. 4620, affirming a decision of the United States Board of Tax Appeals rendered August 7, 1930, which determined deficiencies in petitioner's income taxes for 1924, 1925 and 1926.

[1] Counsel for respondent have advised that this petition will not be opposed, since the Government is filing a similar petition in a similar case, decided against it.

QUESTION PRESENTED

Whether section 219(h) of the Revenue Acts of 1924 and 1926 is unconstitutional as applied to a case where the grantor created an irrevocable trust for the payment of premiums on policies of insurance upon his life and parted with all rights and benefits under such trust and under the insurance policies prior to the enactment of said section of the Revenue Acts.

STATEMENT[1]

"The petitioner, under date of September 18, 1923, executed nine trust agreements for the benefit of his wife, their nine children, and other members and relatives of his family. These trusts were irrevocable for their duration, which was in the first instance until December 18, 1926, with provision for further extension upon notice by the trustor to the trustee. Two such notices have been given and the trusts have been extended to December 18, 1932.

"By the trust agreements, the petitioner transferred to the Wilmington Trust Company, as trustee, the following properties:

(a) Thirty-two insurance policies on the petitioner's life.
(b) Eight hundred and thirty shares of 7 per cent preferred stock of the Christiana Securities Company, a corporation existing under the laws of the State of Delaware.

"The nine trust agreements were in full force and effect during the years 1924-1926 inclusive, and the 32 insurance policies were likewise in full force and effect

[1] As stated in the Board of Tax Appeals' findings.

and held under the terms of the trust during those years.

"The transfer of the insurance policies was absolute and complete. By the trust instruments the trustee was made the owner of such policies and, if the trusts terminated prior to the petitioner's death, all interest in the policies would vest in certain named beneficiaries. The petitioner is not one of such beneficiaries.

"If the petitioner dies prior to December 18, 1932 (or such other date to which the trusts might further be extended), the proceeds of the life insurance policies are to become a trust fund in the hands of the trustee, designated as the Primary Trust Fund. The net income therefrom and the fund itself would be distributed and paid over to named beneficiaries, other than the petitioner or his estate, as indicated in the trust agreements.

"The petitioner retains no right to change the beneficiaries under the insurance policies named in the trust agreements. He has no right to surrender the policies for the surrender values indicated therein, nor to borrow against them. There is no provision under which title to the policies could revest in the taxpayer either at his own discretion or that of him co-jointly with anybody else.

"As to the shares of stock transferred under the trust agreements, the trustee receives the income from the securities, applies the same to the payment of taxes, governmental charges, and incidental expenses including the commissions, and uses the balance of the income for the payment of premiums on the policies of life insurance for the period of the trusts, or so long as the petitioner lives, whichever is the shorter.

"If the trusts terminate prior to the petitioner's death, the securities and any income not paid out, all of which is designated the Secondary Trust Fund, are

to be transferred to the petitioner. If the petitioner dies prior to the end of the trusts, the securities and any net income thereon are to be distributed to the nine children or their issue in the manner specified therein. No part of the Secondary Trust Fund in such case, goes to the petitioner's estate.

"Such is the combined substantive effect of the provisions of the nine trust agreements. To simplify the description of the separate interest of each child dependent upon contingencies, nine distinct trusts (each applying to a one-ninth share in the trust funds) are provided for.

"During the year 1924 dividends from securities transferred to and held by the Wilmington Trust Company as trustee, amounting to $50,422.40, were received by such trustee and, pursuant to the terms of the trusts, were used to pay insurance premiums. During the year 1925 dividends amounting to $50,370.10 and during the year 1926 dividends amounting to $50,422.40 were so received and applied. These amounts have been treated by the Bureau as income taxable to the petitioner and subject to income taxes and surtaxes under the Revenue Acts of 1924 and 1926. This action is based upon the Commissioner's interpretation of section 219(h) of the Revenue Acts of 1924 and 1926.

"The petitioner's wife and all the children beneficiaries of the trust, were living during the years 1924 and 1926, and are still living."

Specification of Errors To Be Urged

The Circuit Court of Appeals erred:

1. In failing to hold the petitioner was not taxable on the dividends received and applied by the trustee to pay insurance premiums pursuant to the terms of the trusts.

2. In failing to hold section 219(h) of the Revenue Acts of 1924 and 1926 unconstitutional as applied to the facts of this case.
3. In failing to reverse the decision of the United States Board of Tax Appeals which decided the case against the petitioner and to remand the case to such Board of Tax Appeals with instructions to enter a decision finding no deficiency in petitioner's income taxes for the calendar years 1924, 1925 and 1926.

Reasons for Granting the Writ

I.

This is one of two test cases (the other being *Wells* v. *Commissioner of Internal Revenue,*[1]) involving a question of considerable public importance which should be settled. Counsel for petitioner knows of twenty cases pending before the Bureau of Internal Revenue on claims for refund, ten cases pending in the Board of Tax Appeals,[2] two cases in the Court of Claims,[3] one case in the Court of Appeals of the District of Columbia[4] as well as the *Wells* case, *supra,* that are dependent upon an ultimate decision of this question. When it is further considered that during the years 1923-1930 inclusive, there was over $4,000,000,000[5] worth of trustee insurance in this country, it seems

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[1] 62 Fed. (2d) ...., C. C. A. 8th, Feb. 4, 1933.
[2] Docket Nos. 41367, 41369, 41370, 46323, 45490, 54279, 60549, 62763, 68377, 69880.
[3] The cases are:
(1) Cummins v. United States, L-337.
(2) Thacher v. United States, L-436.
[4] *Pillsbury* v. *Commissioner*, No. 5407.
[5] 47 Harvard Law Review 896.

highly probable that a great many of these trusts must be affected by the constitutional question involved in this case.

Consequently, until this Court reviews and decides this question of constitutional law, the taxpayers, the Government and lower courts will be in confusion on the subject.

II.

As the Solicitor General has recognized in his petition for certiorari in the *Wells* case, there is a direct conflict in the *ratio decidendi* of the opinions of the Circuit Court of Appeals for the Third Circuit in this case and of the Circuit Court of Appeals for the Eighth Circuit in the *Wells* case.

In the *Wells* case, the court, on the authority of *Hoeper* v. *Tax Commission,*[1] held that since the taxpayer during the taxable years had no ownership of the income he could not be subjected to a tax thereon.

In this (*du Pont*) case, although a similar state of facts existed, the Circuit Court of Appeals avoided the decision in *Hoeper* v. *Tax Commission,* distinguishing it upon the ground that Mr. Hoeper had never owned the corpus from which the taxed income was derived, while Mr. du Pont had at one time owned the corpus.

The Circuit Court of Appeals for the Eighth Circuit based its decision on the *present* legal right to the income. The Circuit Court of Appeals for the Third Circuit based its decision upon *past* rights, which had terminated prior to the enactment of the taxing act.

The obiter language of the Circuit Court in the *Wells* case to the effect that they would have reached the same conclusion as the Third Circuit in the *du*

[1] 284 U. S. 206.

Pont case, was written by the court without any examination of the record in the *du Pont* case and without the benefit of arguments of counsel or examination of briefs. This obiter language is obviously in conflict with the judgment in the case the court was deciding.

III.

It is submitted that the decision of the Third Circuit Court of Appeals in this case is in conflict with the decisions of this Court in *Hoeper v. Tax Commission, supra, and Heiner* v. *Donnan.*[1] The lower court in this case said:

> "While he has neither power over, nor title to, the fund nor a direct financial interest in the insurance policies * * *."

Certainly this is a finding by the court that the petitioner did not own the income produced by the trust corpus[2]—a finding that is justified by the facts of the case. The decision, therefore, is necessarily in conflict with the decisions of this Court in the two above mentioned cases where it was held that A cannot constitutionally be taxed on the income of B. The fact that the corpus may revert to the petitioner cannot justify a distinction between this case and the *Hoeper* case. Suppose A should lease his land to B for three years for a rental of $3,000 which was paid at the time of making the lease. B during that three years raised crops which he sold for a $10,000 profit. Can it be

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[1] 285 U. S. 312.

[2] Note that the court's opinion is obviously inconsistent for while they have in effect found by this statement that the income of the trust did not belong to the petitioner, yet later in the opinion the court states,

"Since it is income to the grantor * * *."

said that A can be taxed on B's profit because at the end of the lease A will receive back the corpus from which the profit was produced?

WHEREFORE, it is respectfully submitted that this petition for a writ of certiorari to review the judgment of the Circuit Court of Appeals for the Third Circuit be granted.

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Of Counsel:
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O. R. Folsom-Jones,
Richard B. Barker.

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CHARLES EL

BRIEF FOR PETITIONER

In the Supreme Court of the United States

OCTOBER TERM, 1932

No. 791

IRENEE DU PONT, *Petitioner*

vs.

COMMISSIONER OF INTERNAL REVENUE.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Third Circuit

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In the Supreme Court of the United States

OCTOBER TERM, 1932

No. 791

IRENEE DU PONT, *Petitioner*

vs.

COMMISSIONER OF INTERNAL REVENUE.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Third Circuit

BRIEF FOR PETITIONER

OPINIONS BELOW

The findings of fact and the opinion of the Board of Tax Appeals (R. 12-15) are reported in 20 B. T. A. 482. The opinion of the Circuit Court of Appeals for the Third Circuit (R. 21-27) is reported in 63 Fed. (2d) 44.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered January 6, 1933. (R. 27.) Petition for a writ of certiorari was filed March 20, 1933, and the writ was granted March 27, 1933. (R. 28.) Jurisdiction is conferred on this Court by Section 240(a) of the Judicial Code as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether section 219(h) of the Revenue Acts of 1924 and 1926 is unconstitutional as applied to a case where the grantor created an irrevocable trust for the payment of premiums on policies of insurance upon his life and parted with all rights and benefits under such trust and under the insurance policies prior to the enactment of said section of the Revenue Acts.

STATUTE INVOLVED

Part of section 219(h) of the Revenue Acts of 1924 and 1926:

> "* * * Where any part of the income of a trust is or may be applied to the payment of premiums upon policies of insurance on the life of the grantor * * * such part of the income of the trust shall be included in computing the net income of the grantor."[1]

STATEMENT

The facts as found by the Board of Tax Appeals (R. 12-14) are as follows:

"The petitioner, under date of September 18, 1923, executed nine trust agreements for the benefit of his

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[1] Section 219(h) and other pertinent parts of section 219 are shown in full in the Appendix, pp. 22 and 23.

wife, their nine children, and other members and relatives of his family. These trusts were irrevocable for their duration, which was in the first instance until December 18, 1926, with provision for further extension upon notice by the trustor to the trustee. Two such notices have been given and the trusts have been extended to December 18, 1932.

"By the trust agreements, the petitioner transferred to the Wilmington Trust Company, as trustee, the following properties:

"(a) Thirty-two insurance policies on the petitioner's life.

"(b) Eight hundred and thirty shares of 7 per cent preferred stock of the Christiana Securities Company, a corporation existing under the laws of the State of Delaware.

"The nine trust agreements were in full force and effect during the years 1924-1926, inclusive, and the 32 insurance policies were likewise in full force and effect and held under the terms of the trust during those years.

"The transfer of the insurance policies was absolute and complete. By the trust instruments the trustee was made the owner of such policies and, if the trusts terminated prior to the petitioner's death, all interest in the policies would vest in certain named beneficiaries. The petitioner is not one of such beneficiaries. If the petitioner dies prior to December 8, 1932 (or such other date to which the trusts might further be extended), the proceeds of the life insurance policies are to become a trust fund in the hands of the trustee, designated as the Primary Trust Fund. The net income therefrom and the fund itself would be distributed and paid over to named beneficiaries, other than the petitioner or his estate, as indicated in the trust agreements.

"The petitioner retains no right to change the beneficiaries under the insurance policies named in the trust agreements. He has no right to surrender the policies for the surrender values indicated therein, nor to borrow against them. There is no provision under which title to the policies could revest in the taxpayer either at his own discretion or that of him co-jointly with anybody else.

"As to the shares of stock transferred under the trust agreements, the trustee receives the income from the securities, applies the same to the payment of taxes, governmental charges, and incidental expenses including its commissions, and uses the balance of the income for the payment of premiums on the policies of life insurance for the period of the trusts, or so long as the petitioner lives, whichever is the shorter.

"If the trusts terminate prior to the petitioner's death, the securities and any income not paid out, all of which is designated the Secondary Trust Fund, are to be transferred to the petitioner. If the petitioner dies prior to the end of the trusts, the securities and any net income thereon are to be distributed to the nine children or their issue in the manner specified therein. No part of the Secondary Trust Fund in such case, goes to the petitioner's estate.

"Such is the combined substantive effect of the provisions of the nine trust agreements. To simplify the description of the separate interest of each child dependent upon contingencies, nine distinct trusts (each applying to a one-ninth share in the trust funds) are provided for.

"During the year 1924 dividends from securities transferred to and held by the Wilmington Trust Company as trustee, amounting to $50,422.40, were received by such trustee and, pursuant to the terms of the trusts, were used to pay insurance premiums. During the

year 1925 dividends amounting to $50,370.10 and during the year 1926 dividends amounting to $50,422.40 were so received and applied. These amounts have been treated by the Bureau as income taxable to the petitioner and subject to income taxes and surtaxes under the Revenue Acts of 1924 and 1926. This action is based upon the Commissioner's interpretation of Section 219(h) of the Revenue Acts of 1924 and 1926.

"The petitioner's wife and all the children, beneficiaries of the trust, were living during the years 1924 and 1926, and are still living."

SPECIFICATION OF ERRORS

The Circuit Court of Appeals erred:

1. In failing to hold the petitioner was not taxable on the dividends received and applied by the trustee to pay insurance premiums pursuant to the terms of the trusts.
2. In failing to hold section 219(h) of the Revenue Acts of 1924 and 1926 unconstitutional as applied to the facts of this case.
3. In failing to reverse the decision of the United States Board of Tax Appeals which decided the case against the petitioner and to remand the case to such Board of Tax Appeals with instructions to enter a decision finding no deficiency in petitioner's income taxes for the calendar years 1924, 1925 and 1926.

SUMMARY OF ARGUMENT

Prior to the first enactment of section 219(h) of the Revenue Acts of 1924 and 1926 the petitioner created trusts irrevocable for their terms, the income to pay premiums upon insurance policies on his life, such policies being in no part the property of the petitioner.

The petitioner, having waived the right to change the beneficiary and transferred his ownership of the insurance policies to the trustee, was in no sense the beneficiary of the trusts. And he had reserved no right to revoke or alter the trusts.

Even if his motive were the reduction of his income taxes, that would not invalidate an otherwise legitimate transaction.

The Government proposes to include in the petitioner's income for 1924, 1925 and 1926 the dividends received by the trustee and applied to the payment of premiums on the insurance policies.

Since petitioner throughout the taxable years involved had no interest in the corpus or income of the trusts and no interest in the life insurance policies, the collection of a tax under section 219(h) of the Revenue Acts of 1924 and 1926 would be unconstitutional, for it would be taxing the petitioner upon income which (a) did not belong to him, (b) was not received by him nor held for future distribution to him, (c) was not derived from his efforts, (d) was not derived from a corpus in which he had any rights, (e) was not subject to his control and was not derived from a corpus subject to his control, (f) did not benefit him in any way, and (g) could not be used by him in payment of the tax asserted with respect to it.

The fact that the petitioner had a reversion in the corpus does not render him taxable on the income during the prior term because the trustee was for the term of the trusts the owner of both corpus and income for uses other than those of the petitioner.

The extension of the trusts from December 18, 1926, was similar to the creation of new trusts, and being for their terms absolute and irrevocable, rendered the corpus and income the property of the trustee, and not

taxable to the petitioner for the reasons mentioned above.

Accordingly, the Court should hold section 219(h) of the Revenue Acts of 1924 and 1926 unconstitutional as applied to the facts of this case.

ARGUMENT

POINT I

Introductory

In 1923 before the enactment of the Revenue Act of 1924 or the Revenue Act of 1926 and before the enactment of any statute containing any provision in any manner resembling subdivision (h) of Section 219 of the Revenue Acts of 1924 and 1926,[1] the petitioner made nine irrevocable deeds of trust by which he conveyed certain property to a trustee. Under the terms of the trusts the trustee was authorized or directed to use the income from the corpus to pay premiums upon insurance policies on the life of the grantor, and the expenses of operating the trust. Income not so used was to be accumulated and to be either transferred to the petitioner at the termination of the trust or in the event of his death prior to the termination of the trust then the unused and accumulated income was to be paid to the beneficiaries of the trust. The petitioner was in no sense a beneficiary of the trusts or of the life insurance policies (for he specifically waived the right to change the beneficiary named in the policies—i. e., the trustee). (R. 12-13.) The petitioner reserved no

[1] And accordingly not within the doctrine of *Milliken* v. *United States*, 283 U. S. 15, 51 S. Ct. 324, and *Klein* v. *United States*, 283 U. S. 231, 51 S. Ct. 398; but rather within that of *Nichols* v. *Coolidge*, 274 U. S. 531, 47 S. Ct. 710, and *Coolidge* v. *Long*, 282 U. S. 582, 51 S. Ct. 306.

right to revoke the trusts or to alter their terms. The conveyance of the corpus of the trusts was absolute for the duration of the trusts. And the ownership of the insurance policies was absolute in the trustee. (R. 13.)

It seems possible that the motive for the creation of these trusts was the reduction of the petitioner's income taxes. But such a motive does not in any manner invalidate an otherwise legitimate transaction and does not constitute tax evasion.[1]

Had the Revenue Act in force at the time the trusts were created carried a provision similar to section 219(h) of the Revenue Acts of 1924 and 1926, it is a fair assumption that the trusts would not have been created.

After the trusts had been in force for some time, the Revenue Act of 1924 was enacted, including in section 219 the following paragraph:

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[1] *United States* v. *Isham*, 17 Wall. 496, *Cf. Clapp* v. *Heiner*, 51 Fed. (2d) 224, 225 (C. C. A. 3rd), where the court said:

> "The contest between the cititzen and his government over taxes will beyond question last as long as that other great struggle with which it is often coupled. To describe its various phases as evasion rather than as avoidance seems to us to use the language of the ultimately victorious contestant rather than to speak as an impartial observer. The artifice or cunning implicit in the first term is not consistent with the approval given by the courts to a disposition of property in the manner best suited to avoid taxation."

and continued with a quotation of the oft cited language of Mr. Justice Holmes in *Bullen* v. *Wisconsin*, 240 U. S. 625, 630.

Compare the remarks of Senator David A. Reed in debating the Revenue Act of 1932 (Cong. Rec., v. 75, p. 11765):

> "It is just like a citizen who comes to a river. He finds two bridges, one a free public bridge and the other a toll bridge. He goes over the free bridge. It can not be said that he is evading the toll. He is taking the method which is not taxable, and he is not resorting to the method that is taxable. Nobody can fairly charge him with evading the tax."

"(h) Where any part of the income of a trust may, in the discretion of the grantor of the trust, either alone or in conjunction with any person not a beneficiary of the trust, be distributed to the grantor or be held or accumulated for future distribution to him, or *where any part of the income of a trust is or may be applied to the payment of premiums upon policies of insurance on the life of the grantor* (except policies of insurance irrevocably payable for the purposes and in the manner specified in paragraph (10) of subdivision (a) of section 214), *such part of the income of the trust shall be included in computing the net income of the grantor.*"

The Revenue Act of 1926 carried the same provision under a similar section number.

In determining income taxes for 1924, 1925 and 1926, the respondent included in petitioner's taxable income the dividends received by the trustee upon the securities which constituted the corpus of the trusts, upon the ground that they fell within the phraseology emphasized in the foregoing quotation. (R. 5-7.) The Board of Tax Appeals upheld the respondent on the same ground (R. 14-15) and the Circuit Court of Appeals affirmed the Board's decision.

POINT II.

Petitioner, at the Time of the Enactment of the Revenue Act of 1924, and Throughout the Taxable Years Involved,[1] Had No Interest in the Corpus or Income of the Trusts.

The deeds of trust were in evidence before the Board of Tax Appeals and their provisions are summarized

[1] Except possibly for the period from December 18 to December 31, 1926.

in the Board's findings of fact. (R. 12-13.) The summaries indicate no reservation of any power to revoke or alter. The Board, in its findings of fact (R. 12) recognizes that they were irrevocable, saying:

> "These trusts were irrevocable for their duration, which was in the first instance until December 18, 1926, with provision for further extension upon notice by the trustor to the trustee. Two such notices have been given and the trusts have been extended to December 18, 1932."

The corpus was the property of the trustee, the income was the property of the trustee, in trust entirely for the benefit of persons other than the petitioner. The petitioner had no power during the period of the trusts to revest in himself any right to any part of corpus or income and he had no measure of control over either.

As Mr. Justice Butler said in *Coolidge* v. *Long*, 282 U. S. 582, 602:

> "The overwhelming weight of authority sustains the conclusion that the succession in the present case was complete when the deed took effect."

The Circuit Court of Appeals in its opinion likewise recognized that the trusts "were irrevocable for their term of duration" and that thereunder the petitioner "transferred * * * certain shares of stock to the trustee" (R. 21) and that "he has postponed his command over funds and policies for three years. While he has neither power over, nor title to, the funds nor a direct financial interest in the insurance policies, yet * * *." (R. 25.)

POINT III.

Petitioner, at the Time of the Enactment of the Revenue Act of 1924, and Throughout the Taxable Years Involved, Had No Interest in the Life Insurance Policies.

It should be noted that although the transfer of the stocks, the income of which was to be used by the trustee for paying premiums, was for a period of three years, subject to extensions, the transfer of the insurance policies was not temporary but permanent and absolute.

The Board of Tax Appeals found as facts that:

> "The transfer of the insurance policies was absolute and complete. By the trust instruments the trustee was made the owner of such policies and, if the trusts terminated prior to the petitioner's death, all interest in the policies would vest in certain named beneficiaries. The petitioner is not one of such beneficiaries. * * * The petitioner retains no right to change the beneficiaries under the insurance policies named in the trust agreements. He has no right to surrender the policies for the surrender values indicated therein, nor to borrow against them. There is no provision under which title to the policies could revest in the taxpayer either at his own discretion or that of him cojointly with anybody else." (R. 12-13.)

The Circuit Court of Appeals recognized that the petitioner "transferred thirty-two policies insuring his life * * * to the trustee. (R. 21.) * * * If the trusts terminate before the death of the petitioner, all interest in the insurance policies will vest in certain beneficiaries of whom the petitioner is not one * * *. If the petitioner dies before the trusts terminate, the proceeds of the insurance policies will become a trust fund to be distributed under the terms of the agreement, and the stock likewise distributed to beneficiaries, other than

the petitioner's estate named in the agreement." (R. 22.)

Where the Court later in its opinion (R. 25) says, "He has postponed his command over funds and policies for three years" and "he has merely postponed his right for the term of the trusts * * * to terminate the existence of the contracts of insurance," it is confusing the temporary trust of the stocks with the permanent transfer of the insurance policies and is departing from the facts as found by the Board and recognized in the early part of its opinion.

POINT IV.

The Collection of a Tax Under Section 219(h) of the Revenue Acts of 1924 and 1926 from the Petitioner Herein Would Be Unconstitutional.

The Commissioner of Internal Revenue is seeking to assess against the petitioner a tax upon certain income although it appears that:

(a) The income did not belong to the petitioner.

(b) The income was not received by the petitioner, nor could it be held for future distribution to him.

(c) The income was not derived from the petitioner's efforts.

(d) The income was not derived from a corpus in which the petitioner had any rights during the taxable years.[1]

(e) The petitioner had reserved no right, either alone or in conjunction with any one else, to revoke or in any way to modify the terms of the trusts.

(f) The petitioner derived no benefit from the income.

(g) The petitioner could not cause any part of the income to be paid to the Collector for the tax.

Accordingly, it is submitted that:

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[1] Except perhaps from December 18 to December 31, 1926.

(a) the case is controlled by *Hoeper* v. *Tax Commission of Wisconsin*, 284 U. S. 206, where the opinion by Mr. Justice Roberts says (p. 215):

> "We have no doubt that, because of the fundamental conceptions which underlie our system, any attempt by a state to measure the tax on one person's property or income by reference to the property or income of another is contrary to due process of law as guaranteed by the Fourteenth Amendment. That which is not in fact the taxpayer's income cannot be made such by calling it income. Compare Nichols v. Coolidge, 274 U. S. 531, 540, 47 S. Ct. 710, 71 L. Ed. 1184, 52 A. L. R. 1081."

That the Fifth Amendment restricts Congress in the same manner that the Fourteenth Amendment restricts the state legislatures is settled in *Heiner* v. *Donnan*, 285 U. S. 312.

In *Knowlton* v. *Moore*, 178 U. S. 41, which involved the interpretation of the War Revenue Act of 1898, where taxes had been collected on certain legacies and distributive shares, the rate being fixed, not on the amount coming to each individual, but on the whole personal estate, this Court condemned such method in these words:

> "But this is equivalent to saying that the principle underlying the asserted interpretation is that the house of A, which is worth only $1,000, may be taxed, but that the rate of tax is to be determined by attributing to A's house the value of B's house, which may be worth a hundredfold the amount. The gross inequalities which must inevitably result from the admission of this theory are readily illustrated."

With the same thought in mind, in *Hartman* v. *Greenhow*, 106 U. S. 642, which involved the validity

of a statute requiring a tax on bonds to be deducted from coupons, which were detached and held by different owners, this Court said:

> "Surely it is not necessary to argue that an act which requires the holder of one contract to pay the taxes levied upon another contract held by a stranger cannot be sustained. Such an act is not a legitimate exercise of the taxing power; it undertakes to impose upon one the burden which should fall, if at all, upon another."

(b) This case is dissimilar to such cases as *Taft* v. *Bowers*, 278 U. S. 470, *Cooper* v. *United States*, 280 U. S. 409, *United States* v. *Phellis*, 257 U. S. 156, etc., for in each of those cases the taxed income was actually received by the person to whom it was taxed, for his own use.

(c) This case is dissimilar to *Lucas* v. *Earl*, 281 U. S. 111, for there the taxed income was Mr. Earl's salary. He was the tree from which the fruit was derived. The court held it proper to tax the salary to him. In our case, the tree was certain corporate stocks over which the petitioner certainly had no control between January 1, 1924, and December 18, 1926.

(d) This case is dissimilar to such cases as *Cohan* v. *Commissioner*, 39 Fed. (2d) 540, *Bing* v. *Bowers*, 26 Fed. (2d) 1017, etc., for in those cases the tax was upheld on the ground that the taxpayers were the owners and in control of the corpus from which the income was derived.

(e) The present case is entirely different from *Reinecke* v. *Smith*—U. S.— (decided by this Court on April 10, 1933.) The *ratio decidendi* in that case was that as a practical matter the settlor of the trust had retained a measure of control in his power to revoke, such power needing only the association of a trustee who had no adverse interest. As Mr. Justice Roberts wrote:

"A settlor who at every moment retains the power to repossess the corpus and enjoy the income has such a measure of control as justifies the imposition of the tax upon him."

In the case at bar, the settlor retained no power to repossess the corpus until December 18, 1926. From the creation of the trust until that date he could avail himself of neither the corpus nor the income for any purpose.

Corliss v. *Bowers*, 281 U. S. 376, and *Porter* v. *Commissioner*—U. S.—(Mar. 13, 1933) are similarly distinguishable.

(f) In such cases as *Old Colony Trust Co.* v. *Commissioner*, 279 U. S. 716, *United States v. Boston & Maine Railroad*, 279 U. S. 732, and *United States* v. *Mahoning Coal Railroad Co.*, 51 Fed. (2d) 208, taxes paid by employers and lessees for account of employees and lessors were treated as additional income to the latter because the payments were made as part of the consideration for services rendered or for the use of property. The courts held that it was reasonable to tax the income to the one who produced it by his efforts or to the one whose property yielded it.

Similarly, in *Adams* v.*Commissioner*, 18 B. T. A. 381, and *Danforth* v. *Commissioner*, 18 B. T. A. 1221, premiums were paid as part of compensation for services and were held taxable to the one who rendered the services so compensated.

In all of these cases the person taxed was either the tree or the owner of the tree, from which the fruit was derived. In the case at bar the fruit was yielded by a tree over which the petitioner had no control, and was collected by another for the benefit of still other persons.

The Board of Tax Appeals and the Circuit Court of Appeals grounded their decisions upon the proposition

that the petitioner benefited from the creation of the trust by relieving himself of the burden of carrying life insurance for his dependents. But he did this by making a gift and parting with the beneficial ownership of the policies (permanently) and of the corpus of the trust fund (for the period of the trust). The fallacy of the argument made by the Government and accepted by the tribunals below—that relief from a moral obligation constitutes taxable income—can be readily seen by applying it to other situations. Suppose a taxpayer felt a moral obligation to provide for his daughter who was about to marry and, instead of giving her an allowance year after year, made her a present of a dowry, the income from which would be sufficient to take care of her. Could it be said that the income which she thereafter received was properly taxable to him because he was relieved of the moral obligation of continuing to support her? Would the situation be any different if he placed the dowry in the hands of a trust company to pay the income to his daughter for life (or for his own life) with a remainder over, retaining no rights in himself?

Hoeper v. *Tax Commission of Wisconsin*, 284 U. S. 206, was not decided upon the ground that the principal which yielded Mrs. Hoeper's income had never been the property of Mr. Hoeper, but upon the ground that it was not his property at the time it yielded the income which was the subject of the tax. Present ownership of the corpus (or a power of disposition thereof equivalent to ownership) may be a basis for the taxation of income, but past ownership of a corpus is no more a proper basis for taxation of income than it would be for the inclusion of the corpus in the taxable estate of a decedent. And, as Mr. Justice Roberts wrote in *Reinecke* v. *Smith, supra*:

"As pointed out in *Burnet* v. *Guggenheim*, No. 283, October Term, 1932, the same considerations as to ownership and control affect the power to impose a tax on the transfer of the corpus and upon the income."

(g) The principle of our graduated income taxes is to vary the burden according to the ability to pay. The tax proposed in this case is based on a theory that wholly disregards this principle. If the settlor should become insolvent, the income of the trust funds would go untaxed, according to the Government's theory for the statute certainly does not give the Government an election to go against the trustee if it fails to collect from the settlor.

However, if section 219(h) should be held unconstitutional an exception to the provisions of section 219(b) would disappear and (under section 219(b)) the income would be taxable to the trustee, by whom it is received and by whom the corpus of the trust is held.

POINT V.

The Fact that the Settlor Had a Reversion in the Corpus Does Not Render Him Taxable on the Income During the Prior Term.

The Board of Tax Appeals has recently had occasion to hold that the ownership of a reversionary interest is not the source of the income during the prior term and accordingly that income should be taxed to the holder of the present estate rather than to the holder of the future estate. *R. E. Nail, et al, Executors*, v. *Commissioner*, 27 B. T. A. 33.[1] The principle is the same in

[1] The Commissioner of Internal Revenue has published his acquiescence in this decision, XII, I. R. B., No. 9, p. 1, and the time for an appeal from the Board's decision has expired.

the case at bar. During the period of the trust the settlor could not subject either corpus or income to his own uses. The income was received by the trustee, the corpus was held by the trustee. The trustee was, for the term of the trust, unquestionably the owner of both corpus and income for the uses mentioned in the trust agreement.

As the Circuit Court of Appeals for the Fifth Circuit said in *United States* v. *Looney*, 29 Fed. (2d) 884, 885:

> "Rents or royalties are included in the income of their owner, though they are not actually received by him, but pursuant to his direction are paid to another. [citations] But rents or royalties are not properly included in the income of one who did not own, receive, or control them; the ownership thereof being vested in another when they accrued."

POINT VI.

The Extension of the Trust from December 18, 1926, Was Similar to the Creation of a New Trust.

Although a statement of the facts necessarily shows that the original trust was created before the enactment of section 219(h) of the Revenue Act of 1924, it is submitted that had the trust been created thereafter, section 219(h) could not be applied to the income thereunder without violating the Constitution. If a man makes an absolute gift of property, even today, it is submitted that the income of that property cannot be taxed to the donor while the property belongs to the donee. When Mr. du Pont extended the trust before it first expired on December 18, 1926, he in effect created a new trust in terms similar to the original trust and everything that has been urged in this brief would be applicable to it.

Section 219(h) can not be justified as a gift tax—it does not measure the tax by the value of the gift. *Heiner* v. *Donnan*, 285 U. S. 312.

The arbitrary nature of the tax and its capriciousness are demonstrated in the Revenue Act of 1932. That Act continues the tax imposed by section 219(h) of the Acts of 1924 and 1926 in the following language:

> "Sec. 167. Income for Benefit of Grantor.
> "(a) Where any part of the income of a trust—
> "(1) is, or in the discretion of the grantor or of any person not having a substantial adverse interest in the disposition of such part of the income may be, held or accumulated for future distribution to the grantor; or
> "(2) may, in the discretion of the grantor or of any person not having a substantial adverse interest in the disposition of such part of the income, be distributed to the grantor; or
> "(3) is * * * applied to the payment of premiums upon policies of insurance on the life of the grantor * * *;
> "then such part of the income of the trust shall be include in computing the net income of the grantor."

Section 501 of the Revenue Act of 1932 imposes a gift tax in the following language:

> "(a) For the calendar year 1932 and each calendar year thereafter a tax, computed as provided in section 502, shall be imposed upon the transfer during such calendar year by any individual, resident or non-resident, of property by gift.
> "(b) The tax shall apply whether the transfer is in trust or otherwise, whether the gift is direct or indirect, and whether the property is real or personal, tangible or intangible; * * *
> "(c) The tax shall not apply to a transfer of property in trust where the power to revest in the

donor title to such property is vested in the donor, either alone or in conjunction with any person not having a substantial adverse interest in the disposition of such property or the income therefrom, but the relinquishment or termination of such power (other than by the donor's death) shall be considered to be a transfer by the donor by gift of the property subject to such power, and any payment of the income therefrom to a beneficiary other than the donor shall be considered to be a transfer by the donor of such income by gift."

Congress, by taxing as gifts the creation of irrevocable trusts (without any exception for trusts to pay insurance premiums), recognizes the completeness of the transfer. By excepting revocable trusts from the gift tax, it recognizes that incomplete transfers should not be taxed as gifts. In the case of revocable trusts it is consistent in taxing the income to the creator of the trusts until such time as he makes the gift complete and ceases to be the owner (actual or potential) of the source of the income.

But in the case of the trust to pay insurance premiums, Congress taxes the grantor on a transfer by gift and then continues to tax him on the income of that gift as if no transfer had been made. It is submitted that this is arbitrary and capricious and a denial of due process of law.

When an irrevocable trust is set up to pay insurance premiums on policies in which no interest is retained by the grantor, it is proper to tax the grantor upon the creation of such trusts if Congress desires to impose a gift tax. But it is improper to tax the income of that trust to the grantor for the reason that it is not his income. As was said by Mr. Justice Sutherland in *Heiner* v. *Donnan, supra*:

"Such an exaction is not taxation but spoliation."

CONCLUSION

It is respectfully submitted that section 219(h) of the Revenue Acts of 1924 and 1926 is unconstitutional as applied to the facts of this case.

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April, 1933.

APPENDIX

Section 219 of the Revenue Act of 1924 and Section 219 of the Revenue Act of 1926 include the following:

"(a) The tax imposed by Parts I and II of this title shall apply to the income of estates or of any kind of property held in trust, including—

"(1) Income accumulated in trust for the benefit of unborn or unascertained persons or persons with contingent interests, and income accumulated or held for future distribution under the terms of the will or trust;

"(2) Income which is to be distributed currently by the fiduciary to the beneficiaries, and income collected by a guardian of an infant which is to be held or distributed as the court may direct;

"(3) Income received by estates of deceased persons during the period of administration or settlement of the estate; and

"(4) Income which, in the discretion of the fiduciary, may be either distributed to the beneficiaries or accumulated.

"(b) Except as otherwise provided in subdivisions (g) and (h), the tax shall be computed upon the net income of the estate or trust, and shall be paid by the fiduciary. The net income of the estate or trust shall be computed in the same manner and on the same basis as provided in section 212, except that—* * *

"(g) Where the grantor of a trust has, at any time during the taxable year, either alone or in conjunction with any person not a beneficiary of the trust, the power to revest in himself title to any part of the corpus of the trust, then the income of such part of the trust for such taxable year shall be included in computing the net income of the grantor.

"(h) Where any part of the income of a trust may, in the discretion of the grantor of the trust,

either alone or in conjunction with any person not a beneficiary of the trust, be distributed to the grantor or be held or accumulated for future distribution to him, or where any part of the income of a trust is or may be applied to the payment of premiums upon policies of insurance on the life of the grantor (except policies of insurance irrevocably payable for the purposes and in the manner specified in paragraph (10) of subdivision (a) of section 214), such part of the income of the trust shall be included in computing the net income of the grantor."

Section 1103 of the Revenue Act of 1924 and Section 1213 of the Revenue Act of 1926 provide:

"If any provision of this Act, or the application thereof to any person or circumstances, is held invalid, the remainder of the Act, and the application of such provision to other persons or circumstances, shall not be affected thereby."

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REPLY BRIEF FOR PETITIONER

In the Supreme Court of the United States

OCTOBER TERM, 1932

No. 791

IRENEE du PONT, *Petitioner,*

v.

DAVID BURNET, *Commissioner of Internal Revenue*

On Writ of Certiorari to the United States Circuit Court of Appeals for the Third Circuit

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In the Supreme Court of the United States

OCTOBER TERM, 1932

No. 791

IRENEE du PONT, *Petitioner,*

v.

DAVID BURNET, *Commissioner of Internal Revenue*

On Writ of Certiorari to the United States Circuit Court of Appeals for the Third Circuit

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REPLY BRIEF FOR PETITIONER

I.

The Government relies on its brief in *Commissioner* v. *Wells,* No. 792, October Term, 1932, for its proposition that section 219(h) of the Revenue Acts of 1924 and 1926 is constitutional when applied to irrevocable trusts. We believe that we have fully answered the Government's arguments in our brief for the respondent in that case as well as in our principal brief for the petitioner in this case.

II.

Unquestionably the settlor retained a reversion (contingent upon his survival) in the corpus of the trust funds. The Government's contention under point II amounts to saying that Congress, if it chooses, may constitutionally tax the income of property to any holder of a future estate therein. The Government's argument under this point is not based on any suggestion that a man can be taxed on the income from property because he once owned the property, but goes to the other extreme and says that he may be taxed on the income of property if he will eventually (on the happening of certain contingencies) own the property. If this be sound, then in case of a limitation to A for life, to B for life, to C in fee provided he survives A and B, otherwise to the heirs of B, Congress would be at liberty, if it saw fit, to tax to C the income received by and held for their own uses by A and B during their lives.

It is true, as said in ***Reinecke*** v. ***Smith,*** (April 10, 1933), that the same considerations as to ownership and control affect the power to impose the tax on the transfer of the corpus and upon the income—in that if there is no power to tax the corpus as a part of a man's estate, there is no power to tax the income from that corpus to that man.

But we submit that this court never intended in ***Reinecke*** v. ***Smith,*** to intimate that because a man had a remote contingent interest in property, which might be taxable as part of his estate, that gave Congress the power to tax all the income from such property to him

prior to the time when he could touch or control the property in any way.

If a conveyance were made to B for the life of A with a power of appointment in A to be effective upon his death, under the authorities the property over which A has power of appointment would be taxable as part of his estate. But the thought that A could be taxed during his life on the income received by B from the property shocks all sense of justice.

The Government says (p. 12):

> "The transfer would also be taxable under the rule applied to revocable trusts in *Reinecke* v. *Northern Trust Co.*, 278 U. S. 339. The only difference between the cases is that there the power to revoke was continuous while here it was periodically recurring—a difference in control which, we believe, is not sufficient to require different results."

The only difference between the cases is the same difference that exists between a term for years and a term at will.

Before the effective date of the Revenue Act of 1924, Mr. du Pont had put it wholly beyond his power to touch, at any time during the calendar years 1924 and 1925, any of the income from the trust funds. He could not subject the income to the tax, nor could he until December 18, 1926 touch the corpus.

This is entirely different from the situation that would have existed if he could have revoked the trusts and used the 1924 income to pay the 1924 tax and the 1925 income to pay the 1925 tax.

He could not even use the 1926 income to pay the

1926 tax, except a very small fraction of it. If the income is presumed to have accrued ratably,[1] he might have subjected to his own use that part accruing in the last thirteen days of the year—13/365ths, or slightly over 3.6%—which would not have helped very much toward the 20% surtax the Government is attempting to collect from him for 1926.

We submit that certainly until December 18, 1926 Mr. du Pont was not, and could not have made himself, the owner of the income or the corpus, and that no income accrued prior to that date can be taxable to him.

When income accrues while the property is owned by one person but is reduced to possession after title has passed to another, Congress may tax that income to the man who owns the property while it accrues—for undoubtedly Congress could levy an income tax under which everybody was required to make returns on an accrual basis, or Congress could tax it to the one who actually received it, as in *Taft* v. *Bowers,* 278 U. S. 470; *Newman, Saunders & Co.* v. *United States,* 36 Fed. (2d) 1009; *Osburn California Corp.* v. *Welch,* 39 Fed. (2d) 41, etc. But, we submit, Congress could not tax to the first owner income which accrued to the second owner and which was received by him, nor could it tax to the second owner income which had actually been received and retained by the first owner and which the second owner could not apply in payment of the tax.

The suggestion of the Government that the taxpayer might render himself immune from taxation by estab-

[1] *Rouss* v. *Bowers,* 30 F (2d) 628, cert. den. 279 U. S. 853.

lishment of trusts renewable from year to year or month to month is probably true. However, analysis of the suggestion of the Government does not startle one to the extent that is inferred by their statement. Suppose A has a 6% $1,000 coupon bond with interest payable semi-annually on January 1st and July 1st. On December 31st of a given year he places the bond in trust for a period of two days, the income of the trust to be payable to his wife. If A were on the accrual basis all but one day of the interest that had accrued since July 1st would be taxable to him and that one day's interest would be taxable to his wife. If A were on the cash receipt basis it is true that he would not, under the present revenue acts, be taxable on the six month's interest but this is because the revenue act allows him to make his return on a cash receipt basis. As suggested above, Congress could require him to report his income on the accrual basis. Consequently, the remedy for the situation propounded by the Government is legislative and not judicial. But if A were on the accrual basis or were required to report his income on the accrual basis, it is submitted that as to one day's interest he could not constitutionally be taxed thereon. By his irrevocable trust of December 31st he parted with all right, title, interest and control over that one day's interest and he could not use that one day's interest income *to pay the tax that would be based on it.*[1]

---

[1] The entire interest income could be taxed to A's wife because she received it. *Taft* v. *Bowers*, 278 U. S. 470. In fact, if A were on the cash receipt and disbursement basis such would be the result under the various revenue acts. Cf. *New York Trust Company, Trustee*, — B. T. A. —, promulgated April 10, 1933. (C. C. H. Dec. No. 7998)

We submit that no matter whether a trust is irrevocable for a day, a month, a year, a lifetime, or forever, there is a constitutional prohibition against taxing to the settlor any income to which he has no title, over which he has no control, if derived from property over which he had no control when the income accrued and was realized.

One of the cases relied on by the Government is *Rosenwald* v. *Commissioner,* 33 Fed. (2d) 423, certiorari denied 280 U. S. 599. In that case the Circuit Court of Appeals for the Seventh Circuit said:

> "Petitioner's chief contention is that there was a completed gift, and that petitioner never received the income.
>
> "It is doubtful whether a holder of securities may separate the income thereafter to accrue from the principal, and make a gift by way of assignment of the income, **without assigning or trusteeing the thing out of which the income arises,** where the effect would be to relieve the donor from a tax he would otherwise be required to pay. **We hold, however, that the delivery to the fund of the negotiable Third Liberty Loan bond coupons, before their maturity, made a completed gift, and that the coupons are not taxable as income as against petitioner.** (Emphasis supplied.)
>
> "* * * If, in the instant case, it must be said that what petitioner did was to give the principal and income therefrom for a period of five years, then, clearly, it seems to us that, as the principal was represented by the stock certificates, the Gimbel note, the lease, and the bonds, there was no reason

why the things assigned could not have been delivered. They could have been delivered to the fund or to a trustee to be held for five years for the purposes of the assignment."

In the case at bar, Mr. du Pont did exactly the things which Mr. Rosenwald had failed to do. He assigned and trusteed the thing out of which the income arose and delivered the stock certificates to the trustee to be held for the period of the trusts.

The Government's attempt (pp. 13-14) to distinguish our citations of cases holding that "income should be taxed to the holder of the present estate rather than to the holder of the future estate" on the ground that those cases were concerned with construction rather than constitutionality of statutes, amounts to an argument that it would be constitutional for Congress to tax the income of a present estate to the holder of a remainder or reversion.

III.

The Government now attempts to justify the tax for 1926 under section 219(g) of the Revenue Act of 1926. This point was not made below, either in the Board of Tax Appeals or in the Circuit Court of Appeals, and the burden should be on the Government to show from the record that the facts on which it relies are true. The record does not show that "It was within the power of the petitioner to revest in himself title to the entire corpus of the trust property during the year 1926." In the light of the language of section 219(g) of the Revenue Act of 1924, the settlor may very

well have decided before the beginning of 1926 to divest himself of the power to terminate the trust and resume title to the corpus during that year.

If the taxpayer did not have the power during 1926 to resume the ownership of the corpus, the income cannot be taxed to him under section 219(g). *Langley* v. *Commissioner*, 61 F. (2d) 796, (C. C. A-2); *Lewis* v. *White*, 56 F. (2d) 390, D. C. Mass., Appeal to C. C. A.-1 dismissed Oct. 21, 1932; *Ashforth Est.*, 26 B. T. A. 1188. If the Government had made the point of section 219(g) in the determination of the Commissioner or before the Board of Tax Appeals, the taxpayer might have been able to show that the trust was extended before the beginning of 1926. But there was no reason why it should have shown that under the Commissioner's determination or the pleadings before the Board, and if the Government now wants to raise the new point it should undertake to show where in the record it appears that the petitioner did in 1926 have the power to revest the trust property in himself.

However, we submit that if we are right in our contention that the ownership of a reversion does not render a man taxable on the income from property which he cannot subject to his own uses, and that Congress cannot tax a man on the income of property of which he has made a gift, it follows, as shown in Point VI of our brief in chief, that the extension of the trust was equivalent to the making of a new gift, the making of which might be subjected to a gift tax,[1] but which

[1] It would have been taxable under the gift tax provisions of the Revenue Act of 1924 or under the gift tax provisions of the Revenue Act of 1932, if it had been made during the effective term of either of those Acts.

would render the income of the transferred property taxable only to the transferee during the term for which the transfer was made.

Respectfully submitted,

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In the Supreme Court of the United States

OCTOBER TERM, 1952

IRENEE DUPONT, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

MEMORANDUM FOR THE RESPONDENT

In the Supreme Court of the United States

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MEMORANDUM FOR THE RESPONDENT

Coincidentally with the filing of the petition for certiorari in this case, the Government filed a petition for certiorari in *David Burnet, Commissioner of Internal Revenue, Petitioner* v. *Frederick B. Wells*, No. —, October Term, 1932. These two cases present an apparent conflict of decision between two circuit courts of appeal upon an important question of constitutional law the decision of which seriously affects the administration of the revenue. We think that the writ should issue in each case and, therefore, do not oppose the petition in this case.

THOMAS D. THACHER,
Solicitor General.

MARCH, 1933.

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BRIEF FOR THE RESPONDENT

OPINIONS BELOW

The opinion of the Board of Tax Appeals (R. 14–15) is reported in 20 B.T.A. 482. The opinion of the Circuit Court of Appeals (R. 21–27) is reported in 63 F. (2d) 44.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered January 6, 1933 (R. 27). The petition for a writ of certiorari was filed March 20, 1933,

and was granted March 27, 1933 (R. 28). The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether Section 219 (h) of the Revenue Acts of 1924 and 1926 may be constitutionally applied to the income of the trusts involved in this case.

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations involved are set forth in the Appendix, *infra*, pp. 17–19.

STATEMENT

The facts found by the Board of Tax Appeals (R. 12–14) may be summarized as follows:

On September 18, 1923, the petitioner created nine trusts for the benefit of his wife and children under the terms of which he transferred to the trustee 830 shares of 7 per cent preferred stock of the Christiana Securities Company, a Delaware corporation, and thirty-two insurance policies on his life. The trusts were irrevocable for their duration of three years with provisions for further extension upon notice by the settlor to the trustee. Two such notices were given and the trusts were extended at least to December 18, 1932. They were in force and effect during the taxable years involved; the policies were then in effect, and all of the beneficiaries of the trusts were living (R. 12, 14).

By the trust instruments the trustee was made the owner of the insurance policies and it was provided that if the trusts terminated prior to the petitioner's death, all interest in the policies would vest in certain named beneficiaries. The petitioner is not one of such beneficiaries and he retains no right to change the beneficiaries. He has no right to surrender the policies for their cash-surrender value or to borrow money on them. There is no provision under which title to the policies could revest in him either at his own discretion or that of him jointly with anybody else (R. 12–13).

If the petitioner should die prior to the termination of the trusts, the proceeds of the life-insurance policies are to become a trust fund in the hands of the trustee, designated as the Primary Trust Fund. The net income from this fund and the fund itself would be distributed to the beneficiaries named in the trust agreements and not to the petitioner or his estate (R. 13).

As to the shares of stock transferred under the trust agreements, the trustee receives the dividends thereon and applies this income after deducting taxes, governmental charges, and incidental expenses, including its commissions, to the payment of the premiums on the policies of life insurance for the period of the trusts, or so long as the petitioner lives, whichever is shorter (R. 13).

If the trusts terminate prior to the petitioner's death, these securities and any income not paid out,

all of which is designated the Secondary Trust Fund, are to be transferred to the petitioner. If the petitioner dies prior to the end of the trusts, this fund is to be distributed to the nine children or their issue in the manner specified and no part thereof is to be distributed to the petitioner's estate (R. 13).

During the year 1924, dividends from securities transferred to and held by the trustee (Wilmington Trust Company), amounting to $50,422.40, were received by the trustee and, pursuant to the terms of the trusts, were used to pay insurance premiums. During the years 1925 and 1926 dividends in the amounts of $50,370.10 and $50,422.40, respectively, were received from securities held by the trustee. These dividends also were used to pay premiums on the life-insurance policies (R. 13–14).

The Commissioner of Internal Revenue asserted deficiencies against the petitioner for 1924, 1925, and 1926 as the result of including the dividends thus applied in the petitioner's gross income for those years. The Board of Tax Appeals sustained the Commissioner's determination and upon appeal the Circuit Court of Appeals affirmed the Board's decision.

SUMMARY OF ARGUMENT

I

Section 219 (h) of the Revenue Acts of 1924 and 1926 is constitutional when applied to irrevocable trusts. The argument on this question is the same

as that presented at pp. 9–21 of the Government's brief in *Commissioner* v. *Wells,* No. 792, October Term, 1932, and need not be repeated here.

II

Section 219 (h) of the Revenue Acts of 1924 and 1926, when applied to the income of property held under a trust indenture which reserves the right to retake the property after three years unless the settlor dies before that time, does not offend the Constitution. Because of his right to retake the property after three years, the settlor retains a substantial interest in the trust fund which affords sufficient constitutional basis for the tax upon the income derived therefrom. In effect the trusts in this case were nothing more than a setting aside of future income without a complete and unqualified transfer of the property producing that income. The petitioner merely "postponed his command" over the trust property. The transfer was incomplete and for estate-tax purposes the trust property could have been included in the settlor's estate if he had died within the period of the trusts. If Congress could impose death duties upon the transfer of the settlor's interest in the trust property upon his death, it could tax the income to him during his life.

We believe therefore that Congress did not exceed its power in providing that the tax on the income of property must be paid by the grantor of the property who retains to himself so great an

interest in it. And this is especially true where the income is applied pursuant to the direction of the grantor and for his purposes.

III

Even though it be held that Section 219 (h) may not constitutionally be applied to all the income in question in this case, the tax asserted for the year 1926 may nevertheless be sustained under Section 219 (g) of the Revenue Act of 1926 (*infra*, p. 19). Income for that year is plainly within the terms of Section 219 (g). The limitation on the settlor's control of the trust property was only temporary, and wholly expired within the taxable year.

ARGUMENT

Section 219 (h) of the Revenue Act of 1924 (*infra*, p. 19), provided that—

> where any part of the income of a trust is or may be applied to the payment of premiums upon policies of insurance on the life of the grantor * * * such part of the income of the trust shall be included in computing the net income of the grantor.

Section 219 (h) of the Revenue Act of 1926 was the same.

The petitioner raises no question regarding the interpretation of this provision. He does not argue that Section 219 (h) is not applicable to irrevocable trusts or that it is not applicable to such trusts created before June 2, 1924, when this pro-

vision was first enacted. On the contrary, the petitioner's sole argument is that Section 219 (h) is unconstitutional.[1]

I

SECTION 219 (h) OF THE REVENUE ACTS OF 1924 AND 1926 IS CONSTITUTIONAL WHEN APPLIED TO IRREVOCABLE TRUSTS

In the Government's brief in *Commissioner* v. *Wells,* No. 792, October Term, 1932, it is contended that Section 219 (h) of the Revenue Acts of 1924 and 1926 is constitutional when applied to the income of insurance trusts which are irrevocable and under the terms of which the settlor has forever parted with title to the fund. For the reasons there advanced, which need not be repeated here, we contend that Section 219 (h) is constitutional when applied to the trusts involved in this case.

If the Government prevails in the *Wells case,* the decision there will be conclusive here. If the tax involved in the *Wells case* is not sustained, we submit that the statute must nevertheless be upheld in its application to the trusts here involved under which substantial property interests were reserved to the settlor. Cf. *Dahnke-Walker Co.* v. *Bondurant,* 257 U.S. 282, 289. Our reasons for this contention, which need not be considered unless the

[1] In the Government's brief in *Commissioner* v. *Wells,* No. 792, October Term, 1932, it is argued (p. 8) that Section 219(h) is applicable to irrevocable trusts and (pp. 22–23) that it is applicable to trusts created before June 2, 1924.

taxpayer prevails in the *Wells case,* are presented below.

II

SECTION 219 (h) OF THE REVENUE ACTS OF 1924 AND 1926 MAY BE CONSTITUTIONALLY APPLIED TO THE INCOME OF PROPERTY HELD IN TRUST WHERE THE GRANTOR OF THE TRUST RESERVES THE RIGHT TO RETAKE THE PROPERTY AFTER THREE YEARS UNLESS HE DIES BEFORE THAT TIME

The trusts involved in this case were created September 18, 1923. They were not final, complete, and unqualified dispositions of property leaving no interest in the grantor, for, although they were "irrevocable for their duration", they continued only until December 18, 1926 (R. 12). If the grantor was living at that time,[2] he had the option to extend the trusts for a further period of three years but it was provided that if he did not choose to extend the period "the securities and any income not paid out * * * are to be transferred to the petitioner" (R. 13). In other words, the petitioner created trusts which were to last for three years, during which time part of the income was to be used for the purpose of paying premiums on insurance on his own life. At the end of any tri-

[2] The chance of the petitioner's dying within the three-year period was very small, so that the transfers were for practical purposes the same as if they had been for three years without qualification. If we assume that the petitioner was 47 years old when the trusts were created (it is stated in Who's Who that Irenee du Pont was born December 21, 1876), the probability that he would survive for three more years according to the American Men Table of Mortality was 0.9710625, or over 97%.

ennium, the trusts were to terminate unless extended by the settlor, and the principal of the trust fund, together with any unexpended income, revested absolutely in the grantor. Thus the settlor retained a substantial interest in the trust property quite apart from the benefit which he derived in having the income applied to pay the premiums on insurance on his own life. In substance and effect it was as if he had established a trust for his life, reserving power to revoke it upon the expiration of each triennium after its creation.

The petitioner seems therefore to be in error in stating in his brief (p. 7) that "The petitioner was in no sense a beneficiary of the trusts", and (p. 9) that the petitioner "had no interest in the corpus" of the trusts. Similarly the statement on p. 12 of the petitioner's brief that "the income was not derived from a corpus in which the petitioner had any rights during the taxable years" and the inference on p. 18 that the transfers were an "absolute gift" seem unfounded. The petitioner retained at all times an interest in the property which was very substantial in extent, an interest which was transferable during the years in question, and which could have been protected in equity if the trustee had failed in any way to recognize it. This interest in the property continued throughout the taxable years here involved. We submit that the petitioner was not deprived of his property without due process of law in being required to pay a tax on the income derived from property in which

he retained so great an interest. It was not an arbitrary, capricious, or unreasonable exercise of legislative power to require the payment of such a tax when the income was applied pursuant to the directions of the settlor and for his purposes.

The trusts in this case were in effect nothing but a setting aside of future income without a complete and unqualified transfer of the property producing that income. It has frequently been held that such a transfer of future income from property is not effective to prevent the income of the property from being taxed to the owner of the property. *Parker* v. *Routzahn*, 56 F. (2d) 730 (C.C.A. 6th), certiorari denied, 287 U.S. 606; *Rosenwald* v. *Commissioner*, 33 F. (2d) 423 (C.C.A. 7th), certiorari denied, 280 U.S. 599; *Dickey* v. *Burnet*, 56 F. (2d) 917, 920 (C.C.A. 8th), certiorari denied, 287 U.S. 606; *Van Meter* v. *Commissioner*, 61 F. (2d) 817, 818–819 (C.C.A. 8th); *Ward* v. *Commissioner*, 58 F. (2d) 757 (C.C.A. 9th); *Leydig* v. *Commissioner*, 43 F. (2d) 494, 496 (C.C.A. 10th); *Porter* v. *United States*, 52 F. (2d) 1056, 1057 (C.Cls.). As the court below said (R. 25), the petitioner merely "postponed his command" over the trust property.

If the owner of property may put its income beyond the constitutional power of Congress to tax it to him by providing through a trust that the income shall be paid for a period of three years to another and that the property shall then revert to him, he would be equally immune from taxation

if he established a trust renewable from year to year or month to month, and the provisions of Section 219 (g) as well as Section 219 (h) would be unconstitutional in their application to the income from such trusts. Plainly, such trusts amount to nothing more than anticipatory dispositions of the future income of property in which the grantor retains substantial ownership. To hold that Congress may not constitutionally tax such income to the person who creates the trust and who retains so great an interest in the trust property would obviously facilitate evasion. Cf. *Lucas* v. *Earl*, 281 U.S. 111.

That the relation which the petitioner retained to the trust property was close enough to support the tax in question is shown by decisions of this Court under the estate tax statutes. In *Reinecke* v. *Smith*, No. 601, October Term, 1932, decided April 10, 1933, this Court said that—

> the same considerations as to ownership and control affect the power to impose a tax on the transfer of the corpus and upon the income.

Under the rule thus announced, considerations as to ownership and control of the trust property sufficient to sustain the power of Congress to require inclusion of the property in the petitioner's estate for estate tax purposes must be accepted as sufficient to sustain the constitutionality of a Federal tax upon the income from the fund.

We cannot doubt the power of Congress to tax the trust fund as part of the settlor's estate in case of his death during the life of the trusts. The trust property was transferred to the trustee for a period of three years only. If the petitioner died within three years, the property was to be distributed by the trustee to named persons. If he survived the three-year period, the property became his absolutely. The transfer was thus plainly within Section 302 (c) of the Revenue Act of 1924 as applied by this Court in *Klein* v. *United States*, 283 U.S. 231. There, a husband transferred property to his wife for life with the provision that if he died before she did the property should be hers absolutely. Here, the property was transferred upon trusts for three years with the provision that if the grantor died within that period the transfers should be absolute. As in the *Klein case* (p. 234), "the death of the grantor was the indispensable and intended event" which was necessary to make effective the ultimate transfer of the trust property to the beneficiaries. The transfer would also be taxable under the rule applied to revocable trusts in *Reinecke* v. *Northern Trust Co.*, 278 U.S. 339. The only difference between the cases is that there the power to revoke was continuous while here it was periodically recurring—a difference in control which, we believe, is not sufficient to require different results. See also *Tyler* v. *United*

States, 281 U.S. 497; *Third National Bank* v. *White,* 287 U.S. 577.

The transfers here were plainly testamentary in form and in substance. For the reasons stated above, in addition to the reasons presented on the similar question at p. 12 of the brief for the Government in *Commissioner* v. *Wells,* No. 792, October Term, 1932, we believe that the trust property would have been taxable as a part of the grantor's estate if he had died while the trusts were in effect.

In view of the fact that the trusts in this case amounted to nothing more than anticipatory arrangements disposing of the future income of property, without any similar disposition of the property itself, and that the transfers would have been taxable as a part of the grantor's estate had he died within the period, we believe it is plain that Congress did not exceed its power in providing that the income from the property should be taxed to the grantor.

For the most part, the petitioner ignores in his brief the effect of the substantial interest which he retained in the trust property. Two cases (*Nail* v. *Commissioner,* 27 B.T.A. 33; *United States* v. *Looney,* 29 F. (2d) 884 (C.C.A. 5th)) are, however, cited in support of the proposition that "income should be taxed to the holder of the present estate rather than to the holder of the future estate" (Br. 17–18). But these cases are plainly inap-

plicable here. They relate solely to the *construction* of the provisions of the statute relating to the taxation of income in ordinary cases (Sections 210 and 211), where, as this Court has held, "ownership" of the income is the principal test. *Poe* v. *Seaborn*, 282 U.S. 101, 109. But no question of construction is involved here. The sole issue raised is that of the *constitutionality* of Section 219(h), which admittedly provides that the income shall be taxed as the Commissioner has taxed it. In view of all the circumstances it seems plain that Congress is not prevented by the Constitution from taxing the income to the petitioner whether he "owned" the income or not.[3]

III

THE PETITIONER IS TAXABLE ON THE INCOME OF THE TRUSTS FOR THE YEAR 1926 UNDER SECTION 219 (g) OF THE REVENUE ACT OF 1926

Even if it be held that Section 219 (h) may not constitutionally be applied to the income in question in this case, the tax asserted by the Com-

[3] The petitioner's confusion of the issues of *construction* and *constitutionality* seems also apparent in the reliance placed on Section 501 of the Revenue Act of 1932 (Br. 19–20). We believe it is obvious that no provision of the Revenue Act of 1932 can affect the *constitutionality* of a statute passed in 1924. Moreover, the petitioner's illustrations fail to show any "capriciousness" even under the Revenue Act of 1932. A tax on the creation of an irrevocable trust and on the income from it are distinct, and Congress may impose both if it chooses. Cf. *Lang* v. *Commissioner*, No. 595, October Term, 1932, decided April 10, 1933.

missioner for the year 1926 may nevertheless be sustained under Section 219 (g) of the Revenue Act of 1926 (*infra,* p. 19). This section provides that—

> Where the grantor of a trust has, at any time during the taxable year, * * * the power to revest in himself title to any part of the corpus of the trust, then the income of such part of the trust for such taxable year shall be included in computing the net income of the grantor.

It was within the power of the petitioner to revest in himself title to the entire corpus of the trust property during the year 1926. The trusts by their terms were to last only until December 18, 1926, and the petitioner then had the option to extend them for a further three-year period. Unless he exercised this option the securities and any accumulated income became the petitioner's property free of the trusts (R. 13).

The situation is, therefore, plainly within the terms of Section 219 (g), and we do not believe that there can be serious question of the constitutionality of this provision as applied to the income for 1926. The validity of Section 219 (g) has been upheld in *Corliss* v. *Bowers,* 281 U.S. 376, and in *Reinecke* v. *Smith,* No. 601, October Term, 1932, decided April 10, 1933. The only distinction between those cases and this is that the settlor's power (subject in the *Smith case* to the consent of another) was continuous throughout the

taxable year while here the power was effective only at one period of time within the taxable year. We do not believe that this distinction is significant. The limitation on the settlor's control over the trust property was only temporary, and wholly expired within the taxable year. We believe that it cannot be said that Congress has no power under the Constitution to tax the income of property to a person who has power within the year to take the property for himself.

CONCLUSION

The decision of the Circuit Court of Appeals is correct and should be affirmed.

Respectfully submitted.

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MAY 1933.

APPENDIX

STATUTES AND REGULATIONS INVOLVED

Revenue Act of 1924, c. 234, 43 Stat. 253, 264, 265, 275:

> SEC. 210. (*a*) In lieu of the tax imposed by section 210 of the Revenue Act of 1921, there shall be levied, collected, and paid for each taxable year upon the net income of every individual (except as provided in subdivision (b) of this section) a normal tax * * *. (U.S.C., Title 26, Sec. 951.)
>
> SEC. 211. (*a*) In lieu of the tax imposed by section 211 of the Revenue Act of 1921, but in addition to the normal tax imposed by section 210 of this Act, there shall be levied, collected, and paid for each taxable year upon the net income of every individual a surtax as follows: * * * (U.S.C., Title 26, Sec. 952.)
>
> SEC. 219. (*a*) The tax imposed by Parts I and II of this title shall apply to the income of estates or of any kind of property held in trust, including—
>
> (1) Income accumulated in trust for the benefit of unborn or unascertained persons or persons with contingent interests, and income accumulated or held for future distribution under the terms of the will or trust;
>
> (2) Income which is to be distributed currently by the fiduciary to the beneficiaries, and income collected by a guardian of an infant which is to be held or distributed as the court may direct;

(3) Income received by estates of deceased persons during the period of administration or settlement of the estate; and

(4) Income which, in the discretion of the fiduciary, may be either distributed to the beneficiaries or accumulated.

(b) Except as otherwise provided in subdivisions (g) and (h), the tax shall be computed upon the net income of the estate or trust, and shall be paid by the fiduciary. The net income of the estate or trust shall be computed in the same manner and on the same basis as provided in section 212, except that—

* * * * *

(2) There shall be allowed as an additional deduction in computing the net income of the estate or trust the amount of the income of the estate or trust for its taxable year which is to be distributed currently by the fiduciary to the beneficiaries, and the amount of the income collected by a guardian of an infant which is to be held or distributed as the court may direct, but the amount so allowed as a deduction shall be included in computing the net income of the beneficiaries whether distributed to them or not. Any amount allowed as a deduction under this paragraph shall not be allowed as a deduction under paragraph (3) in the same or any succeeding taxable year;

(3) In the case of income received by estates of deceased persons during the period of administration or settlement of the estate, and in the case of income which, in the discretion of the fiduciary, may be either distributed to the beneficiary or accumulated, there shall be allowed as an additional deduction in computing the net income of the estate or trust the amount of the income of the estate or trust for its taxable year

which is properly paid or credited during such year to any legatee, heir, or beneficiary, but the amount so allowed as a deduction shall be included in computing the net income of the legatee, heir, or beneficiary.

* * * * *

(g) Where the grantor of a trust has, at any time during the taxable year, either alone or in conjunction with any person not a beneficiary of the trust, the power to revest in himself title to any part of the corpus of the trust, then the income of such part of the trust for such taxable year shall be included in computing the net income of the grantor.

(h) Where any part of the income of a trust may, in the discretion of the grantor of the trust, either alone or in conjunction with any person not a beneficiary of the trust, be distributed to the grantor or be held or accumulated for future distribution to him, or where any part of the income of a trust is or may be applied to the payment of premiums upon policies of insurance on the life of the grantor (except policies of insurance irrevocably payable for the purposes and in the manner specified in paragraph (10) of the subdivision (a) of section 214), such part of the income of the trust shall be included in computing the net income of the grantor. (U.S.C., Title 26, Sec. 960).

Section 219 of the Revenue Act of 1926 (U.S.C. App., Title 26, Sec. 960) is identical with Section 219 of the Revenue Act of 1924, quoted above.

Extracts from the pertinent Treasury Regulations and from the reports of Congressional Committees are set forth at pp. 35–39 of the Government's brief in *Commissioner* v. *Wells,* No. 792, October Term, 1932.

U. S. GOVERNMENT PRINTING OFFICE : 1933

SUPREME COURT OF THE UNITED STATES.

No. 791.—October Term, 1932.

Irenee Du Pont, Petitioner, *vs.* Commissioner of Internal Revenue, Respondent.	On Writ of Certiorari to the Circuit Court of Appeals for the Third Circuit.

[May 29, 1933.]

Mr. Justice Cardozo delivered the opinion of the Court.

This case, like *Commissioner* v. *Wells*, No. 792, decided today, requires us to determine whether Section 219 (h) of the Revenue Acts of 1924 and 1926 is consistent with the Fifth Amendment in its application to trusts for the payment of premiums on policies of insurance.

On September 18, 1923, the petitioner, Du Pont, created nine trusts for the benefit of his wife and children, transferring to the trustee thereby two policies of insurance on his life, and shares of stock in a corporation, the income to be used to keep the policies in force. The trusts were to last for three years, during which term they were to be irrevocable. At the end of the term, they might be extended for a like period at the option of the settlor, and successively thereafter. Two such notices were given, with the result that in 1924, 1925, and 1926, the taxable years involved in this proceeding, the trusts were still in being.

The deeds make provision for the disposition of the policies and separate provision for the disposition of the shares.

As to the policies, the provision is that if the trusts shall be terminated before the petitioner's death, all interest in the policies shall vest in certain named beneficiaries. The petitioner is not one of these, nor has he any power to change them. If the petitioner shall die while the trusts are still in force, the trustee is to collect the insurance, and to hold the proceeds in trust for the use of the beneficiaries named in the agreements.

As to the shares of stock, the provision is that if the trusts shall be terminated before the petitioner's death, the shares and any income not paid out shall be transferred to the petitioner. If,

however, he shall die while the trusts are still in force, the shares are to be divided among the children or their issue.

The Commissioner of Internal Revenue, following the command of Section 219 (h) of the applicable statutes (Revenue Acts of 1924 and 1926; c. 234, 43 Stat. 253; 26 U. S. Code, § 960; c. 27, 44 Stat. 9; 26 U. S. Code App., § 960) made a deficiency assessment by adding to the taxpayer's income the amount expended by the trustee in the preservation of the policies. The Board of Tax Appeals sustained the assessment (20 B. T. A. 482), and the Court of Appeals for the Third Circuit affirmed. 63 F. (2d) 44. A writ of certiorari was granted by this court.

The case is ruled by our judgment in *Burnet, Commissioner* v. *Wells*, No. 792, upholding the validity of the contested statute. If the income of such a trust may be taxed to the grantor though he has retained to himself no reversionary interest in the principal of the trust, *a fortiori* that result must follow where he has made a grant of the estate for a short term of years, reserving the reversion when the term is at an end.

The provisions of these deeds would require a determination in favor of the Government, though *Burnet* v. *Wells* had been decided the other way. "A statute may be invalid as applied to one state of facts and yet valid as applied to another." *Dahnke-Walker Co.* v. *Bondurant*, 257 U. S. 282, 289. Here the grantor did not divest himself of title in any permanent or definitive way, did not strip himself of every interest in the subject matter of the trust estate. During a term of three years, the trustee was to apply the income to the preservation of the policies, and while thus applying the income was to hold the principal intact for return to the grantor unless instructed to retain it longer. The situation in its legal effect would not be greatly different if the trusts had been created for a month or from day to day. One who retains for himself so many of the attributes of ownership is not the victim of despotic power when for the purpose of taxation he is treated as owner altogether.

The judgment is

Affirmed.

Mr. Justice VAN DEVANTER, Mr. Justice MCREYNOLDS, Mr. Justice SUTHERLAND and Mr. Justice BUTLER concur upon the reasons stated in the last paragraph.